University of Alberta

Congress, the Executive, and the Problems of Agency: A Principal-Agent Approach to American Foreign Economic Policy

by

Greg J. Anderson ©

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in

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The undersigned certify that they have read, and recommend to the Faculty of Graduate Studies and Research for acceptance, a thesis titled *Congress, the Executive, and the Problems of Agency: A Principal-Agent Approach to American Foreign Economic Policy* submitted by Greg Jon Anderson in partial fulfillment of the requirements for the degree of Master of Arts in History.

Lawrence Aronsen

David Lightner

Kenneth Norrie

Roderick Macleod

May 21, 1999

To Jacqueline

ABSTRACT

This study applies a principal-agent model of economic theory to the American foreign economic policy process during the late 1980s and early 1990s. The importance of institutional change in the American policy process has long been noted by scholars from several disciplines. However, economists have more recently emphasized the dramatic impact of both formal and informal institutions on economic performance. Although inter-branch, interest group, and bureaucratic politics models of political choice yield important insights into the policy process, a principal-agent approach goes further by demonstrating and explaining the necessary and reciprocal nature of the agency relationship between Congress and the Executive in the policy process. Furthermore, a principal-agent approach provides an economic rationale for policy outcomes in this period that are intentionally different from those that either branch of government could have created individually if given exclusive control over economic policy formation.

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CHAPTER 1

INTRODUCTION AND OVERVIEW

Perhaps no subject in American history has received more public and scholarly scrutiny than postwar U.S. foreign policy. Because the United States has been one of the dominant social, political, military, and economic forces in the twentieth century, identifying, describing, and understanding the sources of American power has been a central preoccupation among academics and public policy practitioners. The immense variety and scope of the literature in American foreign policy defies simple cookie-cutter compartmentalization, primarily because the study of American foreign policy is not the exclusive domain of any single professional or scholarly discipline. Despite the seemingly endless variety and scope of foreign policy literature, the work of most researchers can be lumped into one of three basic categories. First, many scholars have focused on the domestic sources of American policy such as the impact of interest group politics, the operation of government bureaucracies, or the conflict between different branches of government in the American system. Others have developed broader, systemic views of the influences on American policies. This second group of researchers has noted the growing complexity of international relations and pondered the impact of everything from international organizations to the nature of capitalism on American policy formation. Third, many researchers have adopted a more eclectic, some argue more realistic, view of American policy formulation that notes the duality (domestic and foreign sources) of American policies. Whereas scholars espousing systemic views have noted what they believe to be the encroachment of international forces upon national sovereignty and the ability of domestic forces to act autonomously, those that have this more complex view acknowledge the dual, often cooperative role in foreign policy that is played by both

domestic and international influences.

Of particular interest to diplomatic historians, political scientists, and, increasingly, economists, is the interaction between institutions and the American policy process. Several important foreign economic policy studies, such as those by Robert Pastor, I. M. Destler, and Thomas Zeiler have detailed the complex interaction between institutions and the people within them in the overall economic policy processes in different postwar periods.[1] In the last two decades, economists have also turned more of their attention toward institutions by probing the impact of institutional change on economic performance as well as the role of economic performance as an impetus for institutional change. In fact, institutional economics has become one of the most fertile areas of investigation in economics in part because of its central proposition that institutions have a significant impact on economic performance. According to this view, conventional neoclassical approaches to economic theory have become increasingly abstract and have too often sought to identify only optimal economic conditions. The use of such abstract models to predict economic activity has ignored the importance of real life uncertainty created by transactions costs and information asymmetries inherent in economic exchange, or the impact of the institutions whose primary purpose is the reduction of those transactions costs and the mitigation of uncertainty. Coupled with the standard constraints of neoclassical economic theory, institutional approaches to economic performance have sought an understanding of the impact of the humanly devised, and therefore imperfect, social, political, and cultural structures which facilitate, or in some cases hinder, economic activity.

One interesting area of investigation by institutional economists concerns the unique problems associated with a firm's contractual relationship with its employees, contractors, or representatives. Known as principal-agent theory, this approach considers

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[1]Robert A. Pastor, *Congress and the Politics of U.S. Foreign Economic Policy* (Berkeley: University of California Press, 1980); I. M. Destler, *American Trade Politics* (Washington, D.C.: Institute for International Economics, 1995); Thomas W. Zeiler, *American Trade and Power in the 1960s* (New York: Columbia University Press, 1992).

how firms (principals) seek to design institutional changes to their relationships with their employees (agents) which transform the uncertainty associated with information asymmetries, monitoring, and enforcement of agent activities into bearable risk. Because agency relationships are extremely common economic institutions, firms are not the only organizations in which they exist. Whenever an individual depends on the action of another, an agency relationship arises. Whether it is patient-doctor relations, the relationship between investor and financial advisor, or that between shareholders and corporate executives, the basic issue confronting agency relationships is the same: mitigating the uncertainty that results from asymmetric information between principal and agent so as to capture the potential gains from trade.

Agency relationships are also prevalent in the U.S. foreign economic policy process. In the United States, under its Constitutionally delineated separation of powers among the three branches of government, the economic policy process has evolved to include a unique agency relationship between the Legislative and Executive branches. Since 1934, when Congress first delegated its statutory authority over foreign commerce to the President, the foreign economic policy process has been characterized by a delegation of power from the legislature, or principal, to its agent in the Executive. This unique set of circumstances provides scholars with more than half a century of institutional change in the American system that can be used to test principal-agent theory, and presents an opportunity to gain descriptive, explanatory, and predictive insights into the American policy process.

Throughout the twentieth century America's economic institutions have been in a near constant state of evolution. The tumultuous debate over how to alter American trade policies had, until 1934, centered on Congress and its power to set tariff rates. In 1934, the Reciprocal Trade Agreements Act marked the beginning of a revolution in American foreign economic policy that profoundly altered the way foreign economic policy is set. Since 1934, any discussion of institutional change in American foreign economic policy has most often meant altering the agency relationship most responsible for that change, the one between Congress and the Executive.

While institutional change in the American economic policy process has been full of spirited debate in nearly all periods of the postwar era, perhaps no period in recent American history was characterized by more of that debate than the 1980s and early 1990s. America's relative decline as the world's dominant economic power in the postwar period was real, perceived, and, ironically, to a large extent planned. American postwar economic, political, and military support of its postwar allies, as well as the maintenance of U.S. strategic interests in Asia and Europe in many ways facilitated the growth of its own economic competitors. Throughout the postwar period, the United States has regularly engaged in sometimes bitter economic disputes with its allies that often placed American strategic political and domestic economic needs in mutually exclusive positions. However, by the mid-1980s, economic disputes, particularly with Japan and the European Community, had become extremely contentious as the United States languished in one of its worst recessions in a generation and struggled to keep key industrial sectors such as automobiles and steel from disappearing. Added to this mix of economic turmoil at home was the progress towards further trade liberalization that critics saw as exacerbating an already crisis-ridden U.S. economy. The Uruguay Round of the GATT (General Agreement on Tariffs and Trade), the U.S.-Canada Free Trade Agreement, and most controversial of all, progress toward a North American free trade zone at the beginning of the 1990s gave additional impetus to the fierce debate over the future of U.S. foreign economic policy that began in the mid-1980s.

As a result, between 1985 and 1992, American economic institutions encountered some of the strongest pressure for change since the Reciprocal Trade Agreements Act of 1934. For many observers, America's foreign economic policies were in disarray and in dire need of overhaul. As predicted by principal-agent theory, the increasing uncertainty over America's relative economic position contributed to the principal's desire for institutional changes to its relationship with its agent in the Executive that would constrain the agent in the least costly manner available, transform uncertainty into acceptable risk, and achieve a more desirable set of economic outcomes for the United States. The period between 1985 and 1992, illustrates both the historical need for agency in the American

policy process and how agency permits economic policy outcomes that neither Congress nor the Executive alone could have created. Instead of simplistic depictions of the periodic Congressional-Executive battles over trade policy as either periods of Congressional or Executive dominance, or of trade policy formulation as the product of a duel between Capitol Hill protectionists and White House free traders that have been offered by some historians and political scientists, agency suggests an alternative, more parsimonious and sophisticated approach to understanding trade policy. Finally, this period also suggests the utility of agency as a broad foreign economic policy lens to describe, explain, and predict American policy outcomes that incorporates a variety of domestic and international policy inputs and more accurately reflects the essence and complexity of foreign economic policy formulation.

The chapters that follow will highlight the utility of agency as a means of understanding the evolution of American economic policies, their institutional structure, and the significant changes to those structures between 1985 and 1992. Chapter two will review some of the scholarly debate about the sources of American foreign policy generally, and American foreign economic policy specifically. In chapter three a discussion of institutional economics and the problems of agency will emphasize and demonstrate the importance of institutional change to economic performance as well as elaborate upon its applicability to the American policy process. In chapter four, an examination of the United States Trade Representative itself, and as part of institutional change in the larger policy process will serve as a partial demonstration of the efficacy of agency as an explanatory framework. Chapter five will examine the chief legislative byproduct of the economic debate of the mid-1980s, the 1988 Omnibus Trade and Competitiveness Act which transformed the principal-agent relationship between Congress and the Executive, thereby altering the American economic policy process. Chapter six will focus on a specific form of delegation from the principal to its agent in an examination of the 1991 debate over renewal of fast track authority that further highlights the impact Omnibus Act changes had on the agency relationship. Chapter seven will further probe the implications of the 1988 Omnibus legislation by examining its impact on the principal-agent relationship through a

comparison of the two major trade agreements concluded in the period, the U.S.-Canada free trade talks (1985-87) and the North American Free Trade Agreement (1990-92). Chapter eight will briefly address the role played by partisan politics in agency. Lastly, chapter nine will attempt to address potential points of criticism of agency as a foreign economic policy lens and argue further in favor of agency's utility as a means of understanding American foreign economic policies.

From the perspective of the late 1990s, foreign economic policy appears poised to supplant the traditional balance of power strategic military issues that have dominated foreign policy for the past half century. Although large scale military and national security considerations are seldom far removed from ostensibly economic issues, such issues appear to have faded into the distance for the time being as others such as ethnicity, terrorism, human security, the environment and especially economics push themselves to the forefront of national and international agendas. As a result of these issues taking on increased importance, an understanding of the American foreign economic policy process will necessarily facilitate a clearer understanding of the broader American foreign policy agenda. Using agency as a foreign economic policy lens, therefore, is one means of shedding light on American policies for the foreseeable future.

CHAPTER 2

THE FOREIGN ECONOMIC POLICY DEBATE

Few subjects in American history, with the possible exception of the Civil War, have generated more literature than twentieth century American foreign policy. While the foreign policy literature continues to grow at a rapid pace, it originates from an increasingly diverse group of professionals and scholars. In fact, the study of American foreign policy in the twentieth century may be one of the most democratic of subject areas in that persons from a wide variety of backgrounds ranging from the popular media to the diplomatic corps, in addition to academe, have made significant contributions to the foreign policy debate. In fact, some of the most influential contributions to that debate have come from non-academics in the diplomatic corps or related government service. For instance, in February 1946, George Kennan, a career foreign service officer stationed in the Soviet Union, wrote his so-called "Long Telegram" from Moscow which argued for a much tougher and competitive American approach towards the Soviets. His telegram anticipated years of tense Cold War stalemate between the United States and the Soviet Union and was a significant influence on early postwar American foreign policy.[2] Similarly, one of the most influential figures in American foreign economic policy was the career politician and Secretary of State, Cordell Hull. In the mid-1930s, Hull became the chief proponent of liberalizing America's tariff structure in the belief that economic interdependence and prosperity among nations would also promote peaceful relations. This philosophical change in American foreign policy first manifested itself in the 1934

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[2]See George F. Kennan, "The Sources of Soviet Conduct," *Foreign Affairs* 25 (July 1947): 566-82; Melvyn P. Leffler, *The Specter of Communism* (New York: Hill and Wang, 1992), 52-53.

Reciprocal Trade Agreements Act that one historian argued created a "revolution in U.S. trade policy."[3]

The impressive diversity in terms of approach and subject matter found in foreign policy studies is at least in part responsible for the scholarly and disciplinary diversity among researchers based in universities. Where foreign policy was traditionally the domain of diplomatic historians and political scientists, sociologists and even linguists have richly added to the debate.[4] While strategic military and political topics remain integral to the foreign policy debate, several new approaches to foreign relations have augmented our understanding of more traditional approaches. For example, studies examining the role of gender in foreign policy, environmental issues, and the growing influence of non-governmental and transnational organizations in foreign relations have all become important contributions to the broader foreign policy debate.[5]

Scholarship in American foreign economic policy closely parallels that in broader foreign policy studies in terms of variety, but the basic goal of seeking the determinants of

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[3]Alfred E. Eckes, *Opening America's Market* (Chapel Hill: University of North Carolina Press, 1995), 140.

[4]See for example, Paul Hollander, *Anti-Americanism* (New Brunswick, CT: Transaction Publishers, 1995); Noam Chomsky, *Deterring Democracy* (New York: Verso Books, 1991).

[5]See for example, Christine Sylvester, "The Contributions of Feminist Theory to International Relations," in *International Theory: Positivism and Beyond*, ed. Steve Smith, Ken Booth, and Marysia Zalewski (Cambridge: Cambridge University Press, 1996): 254-278; Cynthia Enloe, "Margins, Silences and Bottom Rungs: How to Overcome the Underestimation of Power in the Study of International Relations," in ibid., 202-186; Francis Fukuyama, "Women and the Evolution of World Politics," *Foreign Affairs* (September/October 1998): 24-40; Paul Wapner, "Politics Beyond the State," *World Politics* 47 (April 1995): 311-340; Ellen Dorsey, "Expanding the Foreign Policy Discourse, Transnational Social Movements and the Globalization of Citizenship," in *The Limits of State Autonomy*, ed. David Skidmore and Valerie M. Hudson (Boulder: Westview Press, 1993):237-266; Mark W. Zacher, "The Decaying Pillars of the Westphalian Temple: Implications for International Order and Governance," in *Governance Without Government: Order and Change in World Politics*, ed. James Rosenau and Otto Czempiel (Cambridge: Cambridge University Press, 1992): 58-101.

foreign policy are the same and have led scholars to pose several broad, but important questions concerning foreign economic policy formulation. What are the goals of American foreign economic policy? What is in the national interest? How and over what issues is that national interest to be defined? How, by whom, and through what means is foreign economic policy determined? Although it is difficult to apply any cookie-cutter categorization to the scholarship in this area, the search for the determinants of American foreign economic policy has led researchers to emphasize varying degrees of either domestic or foreign policy inputs. In other words, scholars have focused on foreign policy inputs emanating from domestic sources, foreign or systemic sources, or some mixture of both. For instance, Robert Pastor's important work on U.S. foreign economic policy formation acknowledges many of the competing social and political forces that enter into the policy equation such as interest group pressures, bureaucratic political tensions, political wrangling between Congress and the Executive over policy choices, and even the increasingly important role of international bodies such as the GATT.[6] Yet Pastor concludes that U.S. foreign economic policy can best be viewed and understood as the product of domestic inter-branch wrangling over policy options. Other scholars have been more impressed with systemic factors in the U.S. foreign economic policy process, particularly the nature of capitalist economic systems. Scholars like Immanuel Wallerstein or Andrew Linklater, inspired by Marxist-Leninist literature on the nature of capitalism, have emphasized the exploitative dominance of core, developed countries over the peripheral, or developing world. Coupled with capitalism's predilection toward over-production, the policies of the United States, and other developed world economic powers have, according to these scholars, been driven largely by the need for new sources of raw materials, and market outlets for their production.[7] In a slightly different formulation,

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[6]Robert A. Pastor, *Congress and the Politics*. See also E.E. Schattschneider, *Politics, Pressures, and the Tariff: A Study of Free Enterprise in Pressure Politics, as Shown in the 1929-30 Revision of the Tariff* (New York: Prentice-Hall, 1935).

[7]Immanuel Wallerstein, "The Inter-state Structure of the Modern World-System," in *International Theory: Positivism and Beyond*, 87-107; Andrew Linklater, "The

Thomas McCormick has argued that American foreign economic policies are the product of a collaborative effort between senior (the state and oligopoly capital) and junior (labor and farm interests) economic partners that mitigates some of the traditional divisions between labor and capital by adopting policies that contribute to the broad expansion of economic activity thereby minimizing disputes between these two normally disparate groups.[8] Lastly, a number of scholars have adopted a much more eclectic view of the American foreign economic policy process that combines both foreign and domestic policy inputs. Alfred Eckes, for example, has argued that until the "revolution" in U.S. tariff policy that took place in 1934 when the Reciprocal Trade Agreements Act was passed, and contrary to the late twentieth century belief in the connection between free markets and prosperity, high American tariff rates and economic prosperity were not wholly incompatible. Since 1934, however, the competitive position of American industry has routinely been sacrificed on the alter of national security as U.S. tariff rates were regularly and unilaterally lowered to raise imports, thereby bolstering allied economies and solidifying the postwar western alliance during the Cold War.[9] Similarly, Thomas Zeiler's recent book on the origins of the General Agreement on Tariffs and Trade (GATT) argues that a mixture of Cold War imperatives and Western European economic problems in the early postwar period compelled American leadership to abandon free trade idealism as a postwar objective and offer economic concessions to Cold War allies that were deleterious to U.S. economic interests. Instead of a strong system of open, interdependent markets and prescribed rules for the conduct of trade as originally envisioned in failed organizations like the International Trade Organization (ITO), the system was left with a

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Achievements of Critical Theory," in *International Theory: Positivism and Beyond*, 278-298; See also Joyce and Gabriel Kolko, "American Capitalist Expansion," in *The Origins of the Cold War*, ed. Thomas G. Patterson and Robert J. McMahon, 3d ed. (Toronto: D.C. Heath and Company, 1991): 14-22.

[8]Thomas J. McCormick, "Drift or Mastery? A Corporate Synthesis for American Diplomatic History," *Reviews in American History* 4 (December 1982): 318-30.

[9]Alfred A. Eckes, *Opening America's Market*.

relatively weak GATT system full of exceptions that permitted restrictive national trade policies.[10] Several other scholars of American foreign economic policy, including Robert Pollard and Diane Kunz, have taken similar approaches by emphasizing the competing, and often mutually exclusive, domestic and foreign policy interests that have ultimately shaped American economic policies.[11]

Among the most important academic voices in the foreign economic policy debate are those of economists. Public choice economists in particular have made important observations regarding the formulation of public policy and, therefore, about the sources of foreign economic policy. Like their disciplinary cousins in history and political science, economists have focused on a mixture of domestic and foreign sources of causation in the economic policy process. Anthony Downs, for example, has argued that public policy is the outcome of the rational, self-interested interaction between competing political parties and the public. He has argued that political parties are analogous to entrepreneurs in a profit-seeking economy that produce only those products they believe will result in the highest profits. Political parties, like entrepreneurs producing product lines for market, formulate whatever policy platforms they believe will gain the most votes and give them political power. Rather than carrying out preconceived policies based upon a set of principles, parties formulate policies they believe will accrue for them the benefits of holding office.[12] Other economists have since attempted to apply Down's general views on public policy formation to specific commercial policies. Richard Caves, for example, tested three competing political models for public policy outcomes as explanations for protective Canadian tariff structures up to the 1960s. First, he tested an "adding-machine model"

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[10]Thomas W. Zeiler, *Free Trade Free World: The Advent of the GATT* (Chapel Hill: University of North Carolina Press, 1999).

[11]Robert A. Pollard, *Economic Security and the Origins of the Cold War, 1945-50* (New York: Cornell University Press, 1985); Diane Kunz, *Butter and Guns* (New York: The Free Press, 1997).

[12]Anthony Downs, *An Economic Theory of Democracy* (New York: Harper & Brothers Publishers, 1957).

much like that put forward by Downs where political parties only adopt policies on the expectation that more votes will be gained than lost through such a platform. Second, Caves suggested that tariff policy might be explained through the conscious efforts of government to protect and develop Canadian industry through some form of nationalist policy initiative. Third, and most convincing for Caves, was an interest group model in which individual industries lobby for, and receive, tariff benefits relative to their ability to lobby and their own assessments of the costs and benefits of doing so.[13]

Shortly after Caves' study, G. K. Helleiner addressed the same problem, but from a more complex perspective that took into account international factors such as the effects of successive rounds of tariff reductions under the auspices of the GATT. Helleiner concluded that "unskilled labor intensity was far and away the most significant explanatory variable in the Canadian tariff structure."[14] In other words, those industries employing unskilled labor most intensely had increasingly lobbied for and received protective tariff changes. However, he also concluded that against the backdrop of successive rounds of GATT tariff reduction, competition, and therefore conflict, between transnational enterprises, who generally support tariff reduction, and organized labor groups, that more often do not, was of growing importance to Canadian tariff structures.[15] Given the contemporary late 1990s debate over liberalized trade as well as the increasingly fierce competition between labor and capital over trade policies, Helleiner's 1977 conclusions are particularly relevant.

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[13]Richard E. Caves, "Economic Models of Political Choice: Canada's Tariff Structure," *Canadian Journal of Economics* 9 (May 1976): 278-300.

[14]G. K. Helleiner, "The Political Economy of Canada's Tariff Structure: An Alternative Model," *Canadian Journal of Economics* 10 (May 1977): 325.

[15]Ibid., 318-326; see also D.F. Barnett, "The Galt Tariff: Incidental or Effective Protection?," *Canadian Journal of Economics* 9 (August 1976): 389-407. Barnett demonstrates that between 1858-59, Canadian finance minister Alexander Galt had a clear understanding of the concept of effective protection in that changes made to Canada's tariff schedule helped to protect infant Canadian industry by reducing tariffs on primary inputs while increasing them on finished goods.

Other public choice researchers have narrowed their investigations further by looking at the functions of legislative bodies in the public policy process. Stanley Nollen and Dennis Quinn, for example, revisited Congressional roll call votes during the 100th Congress (1987-88) to compare voting patterns on economic issues with the expected economic and political factors influencing the votes of individual legislators. Nollen and Quinn concluded that factors such as trade policy ideology, regionalism, political contributions from interest groups, positions on key committees, home district unemployment rates, and party affiliation all had some impact on the propensity for members of Congress to take a free trade, fair trade, strategic trade, or protectionist position on trade policy votes. In short, their findings highlight that a mixture of international and domestic factors complicates the simplistic free trade versus protectionism dichotomy used by many scholars to characterize the economic policy process.[16]

Institutional aspects of the legislative part of the public policy process have also been key topics of scholarly investigation. Barry Weingast and William Marshall have examined how non-market forms of exchange in legislatures effectively mitigate many of the problems, such as logrolling, that typically plague the legislative process. Weingast and Marshall argue that, unlike firms, which employ contracts to reduce uncertainty regarding transactions costs, legislatures have no system to ensure that vote trading between legislators is enforceable. Instead, they argue, the legislative committee system found in Congress has evolved into a system of property rights characterized by a seniority system and the division of jurisdiction over certain types of policy (i.e. foreign affairs, finance, armed services) which enforce legislative bargains in a manner similar to contracts in private firms.[17]

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[16]Stanley D. Nollen and Dennis P. Quinn, "Free Trade, Fair Trade, Strategic Trade, and Protectionism in the U.S. Congress, 1987-88," *International Organization* 48 (Summer 1994): 491-525.

[17]Barry R. Weingast and William J. Marshall, "The Industrial Organization of Congress; or Why Legislatures, Like Firms, Are Not Organized as Markets," *Journal of*

Weingast's and Marshall's emphasis on an institutional approach to public policy formation in legislatures suggests the importance of institutions generally in the economic policy process. In fact, a growing body of scholarship has in recent decades begun to focus more exclusively on the role of institutions in American economic policy formation. While a number of earlier studies implicitly acknowledged the importance of institutions and institutional changes to policy outcomes, only in recent decades have scholars begun to address explicitly the impact of institutions.[18] For example, Judith Goldstein has argued that the layered structure of institutions in the economic policy process has resulted in overlapping, often contradictory, currents in American trade policy during the twentieth century. As contemporary constituent interests are pressed upon government policy makers, Goldstein suggests that they are filtered through an existing institutional structure deeply reflective of the economic imperatives and biases of decision makers when the institution was created. If constituent interests contribute to the creation of a new institution to deal with a specific economic problem, it is in effect adding to, rather than radically changing the existing structure. Goldstein suggests that this is a major factor contributing to the coexistence of three apparently contradictory U.S. trade policy positions: first, the belief in the efficacy of free trade; second, an acceptance of state economic intervention in adherence to fair trade principles; and third, a welfare component to trade in which the state redistributes wealth from competitive to uncompetitive industries by means of subsidies, orderly marketing agreements, voluntary export restraints, or tax preferences.[19]

Political Economy 96 (1988): 132-163. See also, Barry Weingast, "The Congressional-Bureaucratic System: A Principle Agent Perspective (with applications to the SEC)," *Public Choice* 44 (1984): 147-191.

[18]See for example, Pastor, *Congress and the Politics*; I. M. Destler, *American Trade Politics*; Steve Dryden, *Trade Warriors* (New York: Oxford University Press, 1995). Each of these authors focuses significant attention on American economic institutions without explicitly describing the impact of them on policy outcomes.

[19]Judith Goldstein, "Ideas, Institutions, and American Trade Policy," *International Organization* 42 (Winter 1988): 179-217; see also G. John Ikenberry, "An Institutional

While the bulk of the foreign policy literature rightly seeks to find the main determinants of foreign policy in a variety of areas, obviously denoting the complexity of the issues involved, both foreign and domestic foreign policy inputs are nevertheless filtered through and altered by the institutions that deal with them. Conversely, many inputs are themselves responsible for altering existing, or sometimes creating new, institutions. As suggested by Goldstein, historical institutional change can tell researchers a great deal about the public policy process. We now turn to a specific form of institutional change and suggest how it can be used to further our understanding of the U.S. foreign economic policy process specifically, but also the foreign policy process on a more general level.

Approach to American Foreign Economic Policy," *International Organization* 42 (Winter 1988): 219-243.

CHAPTER 3

INSTITUTIONS AND ECONOMIC THEORY

In the past two decades, economists have become more aware of the impact of institutions upon economic performance. In fact, institutional economics has quickly become one of the most fertile areas of research within the discipline. However, unlike political scientists or historians who have taken a more descriptive approach to the role of institutions in economic policy, economists have been interested specifically in the economic impact of institutional change and, conversely, how economic conditions themselves alter institutions. One of the central propositions of institutional economists therefore is that institutions matter where economic performance is concerned. Ronald Coase, widely considered one of the originators of an institutional approach to economics, suggested that one of the central problems with mainstream microeconomic theory as presented in academic journals and in textbooks is that it has "become more and more abstract over time, and although it purports otherwise, is in fact little concerned with what happens in the real world."[20] Furthermore, microeconomic theory too readily assumes away the existence of institutional constraints on economic activity or the associated transactions costs. In such a rarefied world, marketplace participants can supposedly obtain, process, and employ perfect information instantly and costlessly.[21]

Institutions, according to Douglas North, "are the humanly devised constraints that structure political, economic, and social interaction. They consist of both informal

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[20]Ronald Coase, "The New Institutional Economics," *American Economic Review* 88 (May 1998): 72; see also Eirik G. Furubotn and Rudolf Richter, *Institutions and Economic Theory* (Ann Arbor: The University of Michigan Press, 1997), xiv.

[21]Furubotn and Richter, *Institutions*, 1, 8.

constraints (sanctions, taboos, customs, traditions, and codes of conduct), and formal rules (constitutions, laws, and property rights)."[22] In the context institutional economics, institutions are separate and distinct from the organizational bodies that subsequently arise to take advantage of institutional structures. Whereas the institutional studies of many other scholars are both descriptive and centered mainly upon formalized organizations, which they often refer to as institutions, institutional economics is concerned with the economic impact of a wider variety of formal, informal, and oft-times intangible, structures and their change over time. The importance of institutions, and the seriousness of their not being explicitly considered within micro-theory is best summed up by Coase:

> The welfare of a human society depends on the flow of goods and services, and this in turn depends on the productivity of the economic system. Adam Smith explained that the productivity of the economic system depends on specialization (he says the division of labor), but specialization is only possible if there is exchange– and the lower the costs of exchange (transactions costs if you will), the more specialization there will be and the greater the productivity of the system. But the costs of exchange depend on the institutions of a country: its legal system, its political system, its culture, and so on. In effect, it is the institutions that govern the performance of an economy. . . .[23]

It may be that institutions are simply *de facto* aspects of economic life, but are they also necessary? The fact is, institutions are integral to economic activity as soon as economic development moves beyond the stage of self-sufficiency. As Coase reminds us, productivity depends upon specialization and with it increased complexity in economic exchange fraught with increasing uncertainty and numerous transactions costs. Were it not for the development of institutions to help guide economic activity, economic actors would be completely lost in a world where the cost and uncertainty of obtaining

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[22]Douglas C. North, "Institutions," *Journal of Economic Perspectives* 5 (Winter 1991): 97.

[23]Coase, "The New Institutional Economics," 73.

information upon which to base economic decisions would virtually prohibit economic exchange. Institutions, therefore, necessarily evolve along with economic specialization and serve to transform the uncertainty associated with imperfect information into risk, thereby reducing transactions costs, and facilitating the capture of the potential gains from trade.[24] Institutions help determine the choice set by which we make economic decisions. Institutions, in essence, are analogous to road maps in that while they do not dictate where we choose to drive, nevertheless structure the choices available to us on our trips. In structuring our choices, institutions therefore also reduce the transactions costs associated with imperfect and asymmetric information by making that information more predictable and easier to obtain.

Although the foregoing implies that institutions necessarily evolve to make economic activity more efficient, in reality there are many examples of *inefficient* institutional change. In fact, there is no necessary reason that institutions need evolve in an efficient way in order to reduce either uncertainty or transactions costs. Like a road map that makes car trips into unfamiliar territory more predictable, and may not necessarily follow the most direct route, institutions, efficient or otherwise, in the same way also serve to reduce uncertainty in economic transactions.[25] One of the best examples of inefficient institutional change that still served to reduce transactions costs is the evolution of the standard typewriter keyboard layout. Although several other layouts have been demonstrated to be much more efficient, the QWERTY layout across the top row of modern typewriters and keyboards became the industry standard and has, despite its objective inefficiency, served to reduce confusion and added transactions costs that might otherwise result from the use of multiple layouts.[26]

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[24]See North, "Institutions," 99-100.

[25]Ibid.

[26]Paul A. David, "Clio and the Economics of QWERTY," *Economic History* 75 (May 1985): 332-337. David recounts that QWERTY became the industry standard through a process equivalent to a polya urn scheme in which an urn is filled with marbles of a variety of color. In a simple scheme of that kind, an urn containing marbles of various

One frequently cited example of institutional evolution and its impact on economic performance involves the general problems associated with common property rights, particularly the so-called tragedy of the commons. Economists observed long ago that individually rational economic decisions can lead to disastrous, irrational outcomes for the collective. One frequently cited example of institutional change in dealing with the tragedy of the commons is the case of cattle ranching on open grazing lands. In this scenario, economically rational cattle ranchers may seek to increase the size of their herds believing that sufficient resources exist on the open range to support them. It is economically rational for a rancher to add additional animals to the open range as long as the private return on doing so continues to be greater than the private cost. However, because the open range contains no means to restrict the entry of other herds, and because other ranchers may also seek to increase herd sizes to maximize profits, the collective impact of increasing numbers of cattle on the open range may be to deplete the range's resources. As ranchers add animals to their herds, both resource depletion and diminishing rates of return throughout the range due to each additional animal become significant problems for all ranchers using the range. In effect, each rancher has perverse incentives. Each is motivated to add more and more animals because he receives the direct benefit of his own animals and bears only a share of the collective costs resulting from resource depletion. The tragedy lies in the disastrous logical end toward which all rationally self-interested ranchers rush– resource depletion and diminishing rates of return to the point where ranching becomes unviable for all.[27]

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colors is sampled with replacement, and every drawing of a ball of a specified color results in a second ball of the same color being returned to the urn. If continued indefinitely, the proportional share of one of the colors will converge to unity. In other words, they will all be one color.

[27]See for example, R. Taylor Dennen, "Cattlemen's Associations and Property Rights in Land in the American West," *Explorations in Economic History* 13 (1976): 423-36; Shawn Everett Kantor, "Razorbacks, Ticky Cows and the Closing of the Georgia Open Range: The Dynamics of Institutional Change Uncovered," *The Journal of Economic History* 51 (December 1991): 861-886; John Umbeck, "The California Gold Rush: A Study of Emerging Property Rights," *Explorations in Economic History* 14

The obvious solution for ranchers on the open range was to control entry of additional herds onto the range. In the period before barbed wire and private property on the range, cattle ranchers achieved this goal through the creation of cattlemen's associations which restricted whose animals could graze on a particular range through the use of branding to identify member animals as well as cooperative round-ups that explicitly discriminated against non-members. This institutional change created a system of property rights that allowed ranchers to restrict access to the open range thereby reducing the rent dissipation and resource depletion normally associated with the tragedy of the commons.[28]

The problems of common property rights on the open range have a parallel in legislative bodies. Self-interested, rational members of Congress intent on re-election seek projects and other benefits for their districts to maximize their chances of re-election. However, the tragedy of the commons enters the equation when other self-interested legislators seek similar perks for their own districts in the presence of finite national resources. Because of majority rule in legislatures, individual law-makers have little hope of garnering enough votes to pass bills that would benefit only their own districts. Vote trading, also called logrolling, is one possible solution to the collective dilemma of legislators as they try to acquire enough support for their own initiatives by agreeing in exchange to vote in favor of the initiatives of others.[29] However, vote trading solves one problem while at the same time creating another: pork-barrel legislation. As individual legislators garner support for pet projects that will benefit their districts and enhance their chances of re-election, other members seek their own projects, ofttimes attaching them to

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(1977): 197-226.

[28]Another example of institutional change in response to the tragedy of the commons is the Newfoundland cod fishery in the nineteenth century. Through the evolution of a futures market-like arrangement between merchants and fishers, known as the Truck System, access to the open fishery was effectively controlled by the merchants that reduced the threat of rent dissipation on the fishery. Rosemary E. Ommer, "'All the Fish of the Post': Resource Property Rights and Development in a Nineteenth-Century Inshore Fishery," *Acadiensis* 10 (Spring 1981): 107-123.

[29]See Weingast and Marshall, "The Industrial Organization of Congress,"137-140.

the same piece of legislation. Like the cattle on the free range, as more pork-barrel items are added to legislative initiatives, the collective bears the burden of any inefficiencies in such legislation.[30] However, this direct parallel needs some qualification. Whereas in the tragedy of the commons on the open range each additional cow directly contributes to the diminishing returns of all ranchers, pork-barrel legislation does not necessarily do the same. Although national resources are finite like the open range, the addition of pork-barrel projects to large legislative bills does not make the legislation inherently inefficient for all. In fact, the addition of infrastructure projects such as dams or roads may be an extremely efficient use of scarce resources, with benefits spread throughout the country. However, as legislative initiatives become fat with the pork-barrel projects of election minded legislators, the odds that inefficient provisions will be added to legislation grows, and along with it, the probability that they will contribute to the burden of inefficiency borne by all.

The most obvious, or at least the most maligned, example of pork-barrel politics is the Smoot-Hawley Tariff Bill of 1930.[31] According to most accounts, re-election minded legislators sought higher tariff rates on individual items of importance to constituents in their districts. The Smoot-Hawley Bill revised tariff schedules on more that twenty thousand items, most of which received increases, and, exacerbated by the price deflation of the 1930s, resulted in the highest American ad valorem equivalent tariff structure in the twentieth century at nearly 60%. While individual districts or sectors of the economy were the direct beneficiaries of protective tariff rates, consumers in particular suffered as the Smoot-Hawley Bill raised the price of imports and contributed to a series of retaliatory tariff revisions by other nations that contributed to an exacerbation of the Great

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[30]See Sharyn O'Halloran, *Process, Politics, and American Trade Policy* (Ann Arbor: University of Michigan Press, 1994), 30-31.

[31]Because tariff bills are technically revenue measures and must originate in the House of Representatives, the correct nomenclature is actually Hawley-Smoot after the authors Representative Willis Hawley (R-Oregon) and Senator Reed Smoot (R-Utah). However, this paper will follow the more common Smoot-Hawley usage. See Eckes, *Opening America' Markets*, 103-105.

Depression.[32] Since then, the ghost of Smoot-Hawley has been repeatedly resurrected as a shining example of how poorly conceived trade policies can lead to economic chaos and even armed conflict as appeared to happen during the 1930s.[33]

Economic history, particularly from an institutional point of view, is the story of economies that either succeeded or failed to evolve institutionally to more effectively, though not necessarily more efficiently, capture the potential gains from economic exchange. Institutional economics has been described as an amalgam of transactions costs economics, property rights analysis, and contract theory.[34] An integral part of contract theory is the principal-agent relationship, also known by itself as principal-agent theory. Principal-agent relationships are pervasive throughout our social, political, and economic lives. Stockholders and management, small businesses and their employees, even patient-doctor relationships all involve some form of agency relationship. Like the cattle ranchers who created a property rights structure to more effectively capture rents on the open range, the American foreign economic policy process has also gone through important, at times dramatic, institutional change in response to changing economic conditions. In the American policy process, the experience of Smoot-Hawley provided the impetus for institutional change that led to the creation of a formal principal-agent relationship between Congress and the Executive in the conduct of foreign economic policy.

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[32]O'Halloran, *Process, Politics*, 32; Destler, *American Trade Politics*, 11-13; Pastor, *Congress and the Politics*, 77-84; E. E. Schattschneider, *Politics, Pressures, and the Tariff*. Contrary to these works, Alfred E. Eckes' *Opening America's Market*, 100-139, argues that Smoot-Hawley in reality did little to exacerbate the Great Depression nor were its tariff rates the highest in American history. Specific tariff rates in Smoot-Hawley were calculated based upon quantity (specific tariffs) rather than on an ad valorem basis. As Depression era price levels dropped, the percentage equivalent (ad valorem rate) of such specific duties soared to near 60%.

[33]One of the best examples of economic policies leading to armed conflict was the rationale for the full scale Japanese invasion of Manchuria in 1937. Due to the impact of the Great Depression on the Japanese economy, Japan throughout the 1930s sought to exert control over the resource rich Chinese province.

[34]Furubotn and Richter, *Institutions*, xiv.

Since 1787, the United States Constitution has clearly delineated the separation of powers among the three branches of government and has been explicit as to their respective jurisdictions. Where foreign economic policy is concerned, the Constitution is again explicit, but also sets the stage for conflict over foreign commerce. Article 1, section 8, assigns Congress exclusive jurisdiction over all foreign commerce, including tariff levies on such commerce. At the same time, article 2, section 2, confers upon the President several key foreign policy powers such as his authority as Commander in Chief of the armed forces as well as the power to negotiate treaties. Therein lies one of the basic conundrums of American foreign economic policy: two separate branches of government, each with a constitutional claim of jurisdiction over international affairs. From well before the Declaration of Independence until the end of the Kennedy Round of GATT negotiations in 1967, tariff rates have historically been one of the most important economic and political issues before American legislators.[35] Tariffs on goods imported into the United States were the single most important source of federal revenue, contributing nearly ninety percent of all revenue as late as 1861.[36]

Throughout the late nineteenth century, law makers and members of the Executive branch fiercely contested the proper means of managing foreign commerce. Throughout most of this period, and well into the twentieth century, Congress cautiously guarded its Constitutional authority over tariff policy. While agents of the Executive branch frequently took the lead in the various reciprocity treaties that were concluded during the nineteenth century, all were considered treaties and, as required by the Constitution, had to be brought before the Senate for final ascent into law. However, in 1890, Secretary of State James Blaine, eager to strengthen the position of the President's negotiating teams and

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[35]Pastor, *Congress and the Politics,* 69. During the Civil War, Congress had to turn to other sources of revenue, such as federal land sales, in order to continue the conflict. As a result, the tariff contributed less than 40% of federal revenue by 1864. Throughout the remainder of the nineteenth and twentieth centuries, the tariff never again accounted for more than 57% (1890) of federal revenue and by 1992 only contributed 1.6%. Source: Eckes, *Opening America's Market*, 46.

[36]Ibid., 73.

improve U.S. access to foreign markets, proposed a radical departure from the standard practice of exclusive Congressional control. Rather than Congress effectively maintaining a final veto over concluded reciprocity treaties when brought before the Senate, Blaine proposed that Congress give the President discretionary authority to conduct negotiations and effect agreements without subsequent Congressional approval. When Congress passed the McKinley Tariff of 1890, which included Blaine's delegation of authority, it set off a firestorm of criticism from several quarters that doubted the constitutionality of delegating commerce powers to the Executive branch. When the debate wound up in the Supreme Court in 1892 (*Field v. Clark*), the Court ruled that such sweeping delegation was in fact constitutional because

> What the President was required to do was simply in execution of the act of Congress. It was not the making of the law. He was the mere *agent* of the law-making department to ascertain and declare the event upon which its expressed will was to take effect [emphasis mine].[37]

Although the McKinley Tariff of 1890 was in effect only four years before its repeal by Congress in 1894, the Supreme Court's decision established a precedent for the use of executive agreements that would dramatically alter American trade policy during the later half of the twentieth century. Forty years after the repeal of the McKinley Tariff, another Secretary of State would win Congressional approval of another, similar grant of legislative authority. The story of Secretary of State Cordell Hull and the philosophical underpinnings of the Reciprocal Trade Agreements Act (RTAA), as well as its broad impact on American foreign policy, is well known.[38] For Hull, the freedom of goods and services to move across borders, thereby creating economic interdependence among

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[37]Quoted in Eckes, *Opening America's Market*, 70-74.

[38]See for example, Pastor, *Congress and the Politics*, 77-93; Alfred E. Eckes, *Opening America's Market* (Chapel Hill: University of North Carolina Press, 1995), 140-177.

nations, was directly related to the maintenance of peace and economic prosperity.[39]

However, issues of international security, economic prosperity, and interdependence were not the only matters of concern addressed by the Reciprocal Trade Agreements Program; so too was the structure of the American foreign economic policy process. Whereas for most of the nineteenth and early twentieth centuries Congress had guarded its Constitutional authority over foreign commerce, the RTAA for the first time gave the Executive branch explicit, statutory, and lasting authority to negotiate with foreign countries and slash tariff rates by up to 50% for a period of five years without returning such agreements to Congress for subsequent approval.[40] On August 24, 1934, the first bilateral trade agreement under the RTAA was concluded with Cuba, marking the beginning of an unprecedented reign by the Executive branch as the most prominent body in American foreign economic policy.[41] The dramatic liberal shift in the orientation of American foreign economic policy spurred by the 1934 RTAA was matched in

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[39]In his memoirs Hull recalled "Toward 1916 I embraced the philosophy I carried throughout my twelve years as Secretary of State, into the Trade Agreements, into numerous speeches and statements addressed to this country and to the world. From then on, to me unhampered trade dovetailed with peace; high tariffs, trade barriers, and unfair economic competition, with war." See Cordell Hull, *The Memoirs of Cordell Hull*, 2 vols. (New York: The MacMillan Company, 1948), 1:211.

[40]The McKinley Tariff of 1890 was not the last important delegation of Congressional authority prior to the RTAA. Technically speaking, delegation continued in the application of "scientific adjustments" to the tariff, often referred to as the flexible tariff, in which authority to investigate and recommend tariff rate adjustments to the President was delegated to the quasi-independent and judicial U.S. Tariff Commission. The provision for a flexible tariff to be determined by the Tariff Commission was included in both the Fordney-McCumber Tariff Act of 1922 and the Smoot-Hawley Act of 1930. The flexible tariff was one of the main reasons that President Hoover supported the Smoot-Hawley bill. Hoover eventually won some discretionary authority over Tariff Commission recommendations, but as the severity of the Depression took hold, Hoover's ability to use the flexible provision to reduce tariff rates became politically untenable. J. Richard Snyder, "Hoover and the Hawley-Smoot Tariff: A View of Executive Leadership," *Annals of Iowa* 41 (1973): 1173-1189; see also Eckes, *Opening America's Market*, 88-90.

[41]See Eckes, *Opening America's Market*, 144.

significance by the dramatic alteration of America's basic trade policy institutions. For the remainder of the twentieth century, the Executive would become an agent of Congress in the foreign economic policy process. It would be the President's job to conclude agreements, adjust tariff rates (within limits prescribed by Congress) and eliminate the potential for destructive pork-barrel tariff setting by Congress. However, while some of the problems associated with logrolling and pork-barrel politics appeared to have been mitigated through the creation of an agency relationship, it also created several others.

There are two basic types of principal-agent relationships. In one form of delegation from principal to agent, as in the delegation of specific responsibilities from a large committee to a smaller one, the interests and motives of both parties are essentially the same. As a result, the threat of opportunistic behavior by the agent and the monitoring costs incurred by the principal are all low. However, in the other form of agency, a grant of authority is given to an agent whose interests are different from those of the principal. Under this later set of conditions, the threat of opportunistic behavior by agents and, therefore, the monitoring costs incurred by the principal rise significantly. As the transactions costs associated with principal-agent relationships rise, the key issue becomes designing a contractual structure between two parties with diverse interests that contains both incentives and restrictions which allow both parties to capture the potential gains from trade.

One of the best examples of the need for agency as well as the problems associated with contractual relationships between parties with opposing interests comes from the evolution of transatlantic trade in the sixteenth through eighteenth centuries. The Hudson's Bay Company, for example, had by the seventeenth century established an expansive fur trading empire around Hudson's Bay in British North America. One of the central problems for the company directors (principals) in London was overcoming the uncertainty regarding the activities of their employees (agents) in North America. Were those agents acting in the interests of the company? How could Company directors in London know? Obviously company directors could not engage in and profit from transatlantic trade by conducting it themselves, so agents in North America were needed

to do it for them. However, the monitoring of agent activities directly would have been both extremely expensive, and highly impractical. How could the principal ensure that its agent acted in the best interests of the Company? What was the solution?

Ann Carlos and Stephen Nicholas have demonstrated that the Hudson's Bay Company experimented with a number of institutional arrangements over the course of many years in response to changing market conditions in an effort to transform the uncertainty and information asymmetries of agency into acceptable risk. One of the main problems for a firm engaged in overseas operations is creating incentives that limit the opportunistic behavior of its agents that are in part the result of information asymmetries between the agent and the principal.[42] Although almost by definition agents typically have information advantages over principals because of their hands-on, practical contact with the economic transactions they were contracted to manage, seventeenth century travel times and great distances exacerbated the problem. In the case of the Hudson's Bay Company, the directors in London concerned themselves with how to ensure agents operating in Canada were not engaged in activities detrimental to company profits, such as smuggling high quality furs back to London on their own account while returning inferior furs on company ships. As Carlos and Nicholas have demonstrated, the Hudson's Bay Company experimented with and employed a variety of methods to limit opportunistic behavior by employees. The Company's employment contracts included such things as efficiency wages, loyalty oaths, and large performance bonuses. In addition to following rigorous accounting procedures, Company officials often recruited heavily from specific English communities to take advantage of kinship loyalties in an effort to further reduce

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[42]Ibid., 179-183; Kenneth J. Arrow, "The Economics of Agency," in *Principals and Agents: The Structure of Business*, ed. John W. Pratt and Richard J. Zeckhauser, (Boston: Harvard Business School Press, 1985): 37-51. Two basic forms of information asymmetry plague those entering into contracts. *Adverse selection* refers to pre-contractual information asymmetry where the agent has knowledge the principal does not, withholds it from the principal, and concludes a contract advantageous to the agent. The *moral hazard* form of information asymmetry occurs post-contract and involves ex post opportunism of agents responding to information obtained in the field.

the potential for opportunistic behavior detrimental to Company operations.[43] Several experiments in institutional change, such as allowing private trapping by employees, were ineffective in preventing opportunistic behavior and gave way to the more practical institutions such as efficiency wages and bonuses.[44]

The Hudson's Bay Company was not the only company engaged in the fur trade, nor did other companies deal with agency in the same way. For example, contrast the experiences of the Hudson's Bay Company with those of the Northwest Company. Not only were Northwest Company operations managed from Montreal, thereby reducing information asymmetries and simplifying monitoring activities, but the company was also operated as a limited partnership rather than as a company with employees as was the Hudson's Bay Company. Whereas Hudson's Bay employees were enticed with efficiency wages and bonuses to ensure efficient operations, the partnership structure of the Northwest Company discouraged opportunistic behavior through incentives such as profit sharing.[45] That the Hudson's Bay Company did not initially employ the most effective means of transforming uncertainty into risk, and that the Northwest Company attained similar outcomes with different methods, suggests that institutional change in principal-agent relationships is common. In fact, as the experience of the Hudson's Bay Company demonstrates, institutional change to its principal-agent relationship was, in part, a series of learning-by-doing experiments in an effort to find what worked.

The experiences of the Hudson's Bay Company in early British North America are not unlike those experienced by the United States Congress in the twentieth century. Since the Reciprocal Trade Agreements Act created the first formal agency relationship between Congress and the Executive in 1934, successive attempts by the principal to alter and

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[43]Ann Carlos and Stephen Nicholas, "Agency Problems in Early Chartered Companies: The Case of the Hudson's Bay Company," *Journal of Economic History* 50 (December 1990): 853-76.

[44]Ibid., 860-65.

[45]Kenneth Norrie and Douglas Owram, *A History of the Canadian Economy*, 2d ed. (Toronto: Harcourt Brace & Company, Canada, 1996), 151-57.

perfect its relationship with its agent have meant that American foreign economic policy institutions have been in a near constant state of evolution. The period between 1985 and 1992 marked one of the most important periods of institutional evolution in American economic policies in recent history.

While Congress and the Executive enjoy both modern communications technology and a relative proximity to one another in Washington, D.C. that reduce the information asymmetries and monitoring costs similar to those experienced by the Hudson's Bay Company in its overseas operations, the basic problems confronting two self-interested bodies with different goals in an agency relationship remain. Although the two branches like to think of themselves as being equal partners in the same cause, the two often work at cross purposes. Because so much of Congressional authority and legislative power deals with domestic issues, and because members have narrow electoral constituencies in their home districts, members of Congress tend to be more responsive to these interests.[46] On the other hand, the President's broader constituency and emphasis on the national interest in foreign policy issues, including economic policy, often pits the two branches against one another. Where trade policy objectives conflict with each other, Congress, in whom ultimate authority over foreign commerce resides, must deal with oversight of its agent.

One of the basic arguments of this study is that the principal-agent relationship suggested by institutional economists is the most appropriate lens through which to understand and explain American foreign economic policies between 1985 and 1992. This study has two major theoretical goals. First, it is a test of economic theory which suggests that when the principal is faced with uncertainty regarding the activities of its agent, it will seek to create incentives or design institutional procedures that constrain the agent in the least costly manner available to ensure that the actions taken by the agent yield, as close as possible, the desired outcome. A second, and more dominant theme of this study is that it seeks to examine and understand one of the more contentious periods in recent American economic history through the lens of principal-agent theory. How and why did the

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[46]See Pastor, *Congress and the Politics*, 53.

principal in this period seek to transform uncertainty about its agent's activities into acceptable risk through institutional change? What specific measures were employed and how did they operate?

The prevailing market atmosphere helps to explain why the principal sought to restrain the agent. During the mid-1980s and early 1990s there was heated debate over a whole series of economic issues ranging from ballooning budget and trade deficits (the so-called "twin deficits"), the perceived loss of American competitiveness (particularly vis-a-vis Japan), the overvalued American dollar, and the disappearance of several mature or "sunset," industries. In the context of the rapidly changing, and increasingly interdependent globalized economy, these issues were frequently at the forefront of the American foreign and domestic policy agendas by the beginning of the 1990s. Agency as a framework for dealing with and explaining American foreign economic policy in this period is appropriate for three reasons.

First, agency is a parsimonious, descriptive, explanatory, and to some extent predictive lens for viewing American foreign economic policy in many different periods. Its elegance stems, in part, from the fact that agency incorporates many of the observations and conclusions of existing theories and schools of thought. For example, because agency focuses upon the interdependent relationship between the principal and its agent, similar frameworks such as inter-branch or bureaucratic politics lenses, which assume a much more adversarial relationship between Congress and the Executive, can be subsumed within an agency framework. However, unlike inter-branch or bureaucratic politics, agency offers a plausible economic, rather than purely political, or *ad hoc* rationale for the interaction between principal and agent that results in policy formation.

A second, and related, argument in favor of agency is that unlike Congressional or Executive dominance decision-making models that depict Congress and the Executive as being in a pitched battle over mutually exclusive positions, agency offers a more benign explanation for compromise that explains why in the midst of the mid-1980s and early 1990s acrimony over American economic policies and pressure to adopt nationalistic policies, American policy retained its essentially liberal orientation despite what many have

argued has been an aggressive and unilateral shift in American trade policy in favor of "process protectionism" as embodied in the use of measures such as voluntary export restraints, voluntary import expansion agreements, as well as its countervail and anti-dumping laws. This assertion helps explain the findings of scholars such as Robert Pastor and I. M. Destler who have demonstrated that in spite of periods of American economic decline relative to other developed nations in the late twentieth century, U.S. economic policies have remained remarkably liberal.[47]

Third, and most interestingly, agency helps explain why the American foreign economic policy process regularly manages to come up with "middle ground" policy choices. Whereas inter-branch politics models suggest that middle ground policies are the product of bitter debate and compromise, agency asserts that through the deliberate delegation to an agent, the American system generates policy options and outcomes that neither Congress nor the Executive could have created had either been left to formulate them on their own.

Changes to the contractual principal-agent relationship between Congress and the Executive in four key areas of the American foreign economic policy equation in the late 1980s and early 1990s serve to demonstrate the utility of using agency as a foreign policy lens and form the major organizational components of this study. In chapter four, I will focus on the United States Trade Representative and its changing role in the American policy process from its inception in 1962 to the present. Chapter five will examine one of the most important pieces of trade legislation in the postwar period, the 1988 Omnibus

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[47] Pastor, *Congress and the Politics*, 186-99; I. M. Destler, "U.S. Trade Policy in the Eighties," in *Politics and Economics in the Eighties*, ed. Alberto Alesina and Geoffrey Carliner (Chicago: University of Chicago Press, 1991), 252-3. The tremendous economic prosperity enjoyed by the United States in the late 1990s relative to other developed economies in Europe, and particularly Asia, seems to undermine, at least temporarily, fears of America's relative economic decline expressed by commentators such as Clyde Prestowitz and the economist Lester Thurow. See Lester Thurow, *Head to Head: The Coming Economic Battle Among Japan, Europe, and America* (New York: Morrow, 1992); Clyde Prestowitz, *Trading Places: How We Allowed Japan to Take the Lead* (New York: Basic Books, 1988).

Trade and Competitiveness Act, and highlight its role as a major impetus for institutional change in the principal-agent relationship during this period. Chapter six, will focus on the battle over a specific form of delegation of authority from the principal to its agent, fast track authority, during the debate over its extension in 1991. Finally, chapter seven will examine how institutional changes to the principal-agent relationship made by the 1988 Omnibus legislation affected the outcomes of the two major trade agreements initiated in the period– the United States-Canada Free Trade Agreement (FTA), and the North American Free Trade Agreement (NAFTA).

CHAPTER 4

THE UNITED STATES TRADE REPRESENTATIVE

In 1934, when Congress delegated its authority over the regulation of foreign commerce to the Executive branch, the Department of State was assigned primary responsibility for conducting trade negotiations. Centralizing responsibility for trade within the Department of State in effect hid a significant portion of trade policy activity from public, and to some extent Congressional, scrutiny. Successive Congresses continued to endorse delegation to the Executive in the early postwar period, although both the longevity and depth of tariff cutting authority extended to the President were curtailed.[48] However, by the early 1960s, the signs of slippage in America's postwar economic dominance were emerging.[49] Congressional and private sector interests were increasingly expressing dissatisfaction with State Department trade policies which they saw as unsympathetic to domestic interests and preoccupied with foreign policy objectives.[50] With trade policy-making concentrated within the inherently secretive Department of State, Congress lacked effective oversight of policies that were both increasingly important to American economic prosperity and well within the authority given Congress by the Constitution. Also within the jurisdiction of Congressional authority is the ability to "make all laws which shall be necessary and proper" for executing its Constitutional powers.[51] In

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[48]See O'Halloran, *Process, Politics*, 128-37; Pastor, *Congress and the Politics*, 84-104.

[49]See Thomas Zeiler, *American Trade & Power*, 21-46.

[50]Pastor, *Congress and the Politics*, 112, 168; O'Halloran, *Process, Politics*, 146.

[51]*U.S. Constitution*, article 1, section 8.

1962,Congress did just that by creating the Special Trade Representative(STR). When President Kennedy's Trade Expansion Act was being considered by Congress that year, legislators included a provision within the final bill that shifted primary responsibility for trade negotiations away from the State Department by expanding and clarifying the rules for Congressional consultation and conspicuously placing the STR within the Executive branch. However, as written, the 1962 Trade Expansion Act was vague about the size or precise location of the STR. It was not until January 1963 that Executive Order 11075 actually placed the STR formally within the Executive Office of the President.[52]

In 1974, the official title of the Special Trade Representative was changed to the United States Trade Representative (USTR), its status enhanced by transforming it into a cabinet-level agency within the Office of the President, and bolstered further in 1980 by assigning the USTR the rank of Ambassador to major international trade organizations like the GATT. Furthermore, changes in 1980 also codified the USTR's position as chief U.S. trade negotiator and placed the Office in charge of the overall coordination and administration of trade policy.[53] One of the main reasons for creating the USTR at all was to constrain Executive discretion on trade policy by making policy activities more transparent to both Congress and the public. A less obvious, and not necessarily planned, result of these changes was the mitigation of some of the information asymmetries that gave an advantage to the agent in U.S. policy formation. By placing what was in effect a

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[52]O'Halloran, *Process, Politics*, 93-4; 146-7. See also Destler, *American Trade Politics*, 107. See also Steve Dryden, *Trade Warriors* (New York: Oxford University Press, 1995), 52-59. Dryden suggests that the idea for a Special Trade Representative came from House Ways and Means Committee Chairman, Willbur Mills (R-Arkansas) mainly because of his dissatisfaction with State Department handling of trade matters. Ironically, the first Presidential appointment to the new post was former Secretary of State, Christian Herter.

[53]See Office of the United States Trade Representative, *The Office of the United States Trade Representative, Mission* at http://www.ustr.gov/history/index.html; Internet; accessed April 26, 1999; and Office of the United States Trade Representative, *History of the Office of United States Trade Representative* at http://www.ustr.gov/mission/index.html; Internet; accessed April 26, 1999.

Congressional representative within the Executive Office of the President and assigning him or her cabinet level status, Congress had, in effect, tried to reduce the potential for opportunistic behavior that daily contact with foreign governments on trade issues had afforded the State Department since 1934. By placing a cabinet-level official within the Executive branch, directly accountable to both Congress and the President, early problems with oversight of the delegation of authority to an agent appeared to have been solved. Yet by maintaining the basic delegation of authority to the Executive and by creating a new trade policy body within the Executive rather than resuming control over trade as it had done prior to and during the Smoot-Hawley era, Congress was still acknowledging the continuing need for a principal-agent relationship on trade matters.[54]

In spite of these changes to the principal-agent relationship, considerable uncertainty over foreign commerce persisted well into the 1980s. Although located within the Executive Office of the President, the USTR has enjoyed only periodic support from the President. Perhaps seen as a Congressional spy of sorts, the USTR has by and large remained at arms length from the inner-circle of cabinet. While Kennedy reluctantly acceded to a reorganization of the Executive in 1962, he viewed the creation of the STR

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[54]Prior to 1934, Congress did not always assume direct control over tariff setting. Provisions within the McKinley Tariff actually delegated significant authority to the President (See pages 19-21). The 1930 Smoot-Hawley Tariff Bill, also delegated authority through its "flexible tariff" provisions in which the quasi-independent and judicial International Tariff Commission could investigate and recommend to the President alterations in specific tariff rates. Some scholars have argued that President Hoover has been unfairly maligned for signing Smoot-Hawley and argue that he fought for, and may. have signed the bill only because it contained, "flexible tariff" provisions. See Eckes, *Opening America's Market*, 134-5; Pastor argues that the flexible tariff was a disaster both conceptually and practically. One purpose of specific tariffs is to protect domestic industry by equalizing production costs vis a vis foreign producers. However, with tariff lists of several thousand items, the Tariff Commission worked at a rapid pace yet only managed to complete reports on thirty eight items between 1922 and 1930. In addition, since the purpose of trade is to take advantage of cost differentials (comparative advantage), trying to equalize costs defeats the purpose of trade. See Pastor, 77-83; See also, J. Richard Snyder, "Hoover and the Hawley-Smoot Tariff," 1180; William Starr Myers, *The Foreign Policies of Herbert Hoover: 1929-1933* (New York: Charles Scribner's Sons, 1940). 127.

largely as a form of appeasement to protectionist elements on Capitol Hill rather than as a serious policy player.[55] During the Nixon years, the USTR became a sort of "bureaucratic backwater" as the heads of other agencies sought to wrestle away some of the USTR's responsibilities. On top of this, considerable pressure was exerted by high ranking Nixon Administration officials to eliminate the USTR altogether.[56] Even after the position of the USTR within the Executive was further codified and strengthened in 1974, acceptance of the USTR as a bridge between Congress and the Executive, or as a substantive policy organ, was slow and Presidential attention to it infrequent.

In the mid-1980s, bureaucratic power struggles within the Executive continued to create confusion over who was to take the lead on trade issues. In addition to the USTR, the Departments of Commerce, Treasury, Agriculture, and State, as well as the U.S. International Trade Commission, all had significant roles in the overall trade policy equation. During the first Reagan Administration, for example, disputes between Commerce Secretary Malcolm Baldrige and the USTR over jurisdiction on trade issues became commonplace.[57] Presidential ambivalence toward trade issues, and the USTR in

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[55]See Zeiler, *American Trade and Power*, 155; Destler, *American Trade Politics*, 106, 121; Dryden, *Trade Warriors*, 52-60. Dryden recounts that Kennedy "was concerned about the implications of having controversial trade decisions made on his doorstep . . . but that it was later decided putting trade in the White House would 'permit better control' and decrease the squabbling among the Cabinet departments concerned with trade."

[56]Steven Dryden, *Trade Warriors*, Chapter 7. By the time President Nixon's STR nominee, Carl Gilbert, was confirmed by the Senate in late July 1969, the STR's position had been unoccupied for six months. Soon after his confirmation, Gilbert suffered a heart attack that left him out of action until October; an event completely hidden from the White House by STR staffers. Dryden argues that these events, coupled with the secretive and exclusive nature of the Nixon Administration's inner circle of decision making restricted primarily to State Department and National Security Council staff, allowed these and other agencies, such as the Commerce and Treasury Departments, to assert themselves into areas normally handled by the STR. So isolated was Gilbert from trade policy decisions that he and Nixon never had a personal meeting during Gilbert's two year tenure as STR. See also Destler, *American Trade Politics*, 108.

[57]Destler, *American Trade Politics*, 118-20.

particular, coupled with the rapidly deteriorating balance of trade and exploding budget deficits, contributed to the growing feeling on Capitol Hill that American trade policy was a rudderless ship. The Office of the USTR, created to add transparency to the principal-agent relationship, was also often caught in the middle during Congressional-Executive disputes over trade policy. On one hand, the USTR was part of the Executive branch, but also the victim of Presidential ambivalence as to its role in the policy process, and from time to time even its existence. On the other hand, despite being the brainchild of Congress, the USTR was still part of the Executive branch and found few friends on Capitol Hill during the 1980s. In fact, as foreign trade relations with countries like Japan and the European Community deteriorated throughout the 1980s, an alarmed Congress frequently vented its frustration on the Executive's most visible symbol of administration trade policy; the Office of the USTR.

In August of 1986 during hearings before the House Foreign Affairs Subcommittees, Peter Murphy, the USTR's point man in the United States-Canada Free Trade talks was given a rough ride by Representatives over Administration practices. Following repeated assurances by Murphy that the Administration intended to consult with Congress at every step of the way during the Canada talks and that no issue, especially Canadian subsidy and dumping practices, had been precluded from the negotiating table, Murphy faced some harsh criticism.[58] When questioned by Robert Lagomarsino (D-California) as to the substantive details of talks with Canadian negotiators, Murphy unintentionally highlighted one of the basic problems with agency that Congress was trying to solve with the creation of the USTR: the principal's monitoring of agent activities.

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[58]Statement of Peter Murphy, Special Negotiator for U.S./Canada Affairs, Office of the United States Trade Representative, in U.S. Congress, House, Subcommittees on International Economic Policy and Trade and on Western Hemisphere Affairs, *United States/Canada Trade Relations, Hearing Before the Subcommittees on International Economic Policy and Trade and on Western Hemisphere Affairs of the Committee on Foreign Affairs*, 99th Congress, 2nd session, August 12, 1986, 5-7.

> Well, we haven't gone into the details because in essence we believe that the meetings are discussed in private because if you negotiate in public, in my view, you aren't going to get very far anyway, because somebody is going to say they have a problem with it. . . . From my standpoint, you know, you can't go into these meetings not knowing where you want to go and not having any kind of idea of the sense of the private sector and the sense of the administration, and you have to work these things out well in advance to these individual meetings.[59]

The mutual exclusivity of seeking public input yet conducting talks away from the oversight of Congress or the public prompted Representative Bereuter (R-Nebraska) to suggest that if "this was a parliamentary system, I would cast a vote of no confidence against the administration."[60] Bereuter then gave Murphy a lecture on the proper lines of communication between Congress and the Executive saying,

> I think this administration has failed us and failed the American people, as has the previous one, very badly. The Constitution gives the responsibility for the regulation of international commerce to the Congress. This is not an Executive function you are pursuing, Mr. Murphy, and I am sure you are aware of that, but I think it needs to be reinforced from time to time. It is our responsibility, and I think that the kind of input that you need from Congress to see how we feel about this, ought to come at the beginning of the process or you are going to run into deep, deep, trouble when you come here with any kind of agreement that you do negotiate. It is the reverse order. You come to us first, not afterwards.[61]

Congressional dissatisfaction over talks with Canada was only one manifestation of the general displeasure of the principal with its agent's actions. As was the case in 1962 when the USTR was created, Congressional dissatisfaction with trade policy in the 1980s was giving impetus to renewed proposals for a further reorganization of the Executive. In other words the principal was again looking for ways to constrain the behavior of its agent. However, in the opinion of former USTR Robert Strauss, altering agent behavior

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[59]Ibid., 21-22.

[60]Ibid., 23.

[61]Ibid., 23-4.

did not necessarily have to come in the form of a radical alteration of the principal-agent relationship. As Strauss testified before the Finance Committee,

> it is in the process of devising legislation that the Congress and the Executive branch, in consultation with the private sector, will find and articulate a coherent trade policy for this country. The process of legislating will focus attention on trade and impose a time frame in which a consensus must be reached.[62]

One consistent shortcoming of the 1962 creation of the USTR is that while it created a body to assist with trade policy coordination, it did not concentrate the delegation of Congressional power over foreign commerce in one office. As noted above, Treasury, Commerce, Agriculture, and State all had a hand in formulating overall trade policy. The need for a more coherent, single-minded approach to policy coordination was reflected in renewed calls for Executive reorganization where all powers related to foreign commerce would be concentrated in a new Department of International Trade.[63] However during his testimony before the Senate Finance Committee, Strauss defended the relevance of the USTR saying that "one of the great defaults we have had in the trade area was the failure of the Administration to more effectively use Bill Brock in his capacity as STR[1981-85]."[64] Rather than seeking an entirely new bureaucratic structure, Strauss

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[62]Statement of Mr. Robert Strauss, Akin, Gump, Strauss, Hauer & Feld, Washington, D.C. (Former USTR 1977-79), in U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st session, January 13, 1987, 36.

[63]Destler, *American Trade Politics*, 109, 118-120; Dryden, *Trade Warriors*, 288-291. Some of the loudest calls for Executive reorganization came from within the Administration itself in the early 1980s, particularly Reagan advisor Edwin Meese and Commerce Secretary Malcolm Baldrige. The Baldrige proposal called for the merger of the USTR with the Department of Commerce into a new Department of International Trade and Industry (DITI). Both the name and purpose of DITI were very similar to the Japanese Ministry of International Trade and Industry (MITI) with whom the United States was engaged in a bitter dispute over auto trade in the early1980s.

[64]See Robert Strauss in U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st

believed that the existing institutional structure was more than adequate. "A new Department of Trade doesn't really do a damned thing unless it is done with a purpose of making us able to act more effectively and deal with problems more substantively."[65] During the Ford Presidency, Strauss claims that as USTR he "had every tool [he] needed and the support."[66] The most important institutional problem that needed to be addressed by Congress was developing the tools necessary to eliminate the periodic ambivalence toward established trade policy procedures and the USTR by the President. Among the most damaging effects of periodic ambivalence and bureaucratic infighting for control of trade policy within the Executive has been the lack of institutional memory and expertise within the USTR's office that might otherwise have made the office a consistently effective advocate for American trade interests.[67]

Just over a month after Strauss' testimony, and again in front of the Senate Finance Committee, Treasury Secretary James A. Baker III, and then current USTR Clayton Yeutter faced a similar, but much more hostile, gauntlet of tough questions about U.S. trade policies. Amid familiar warnings from Senators about where ultimate authority for trade policy rests and the need for greater Administration consultation with Congress, USTR Clayton Yeutter retorted that

> Consultation is one thing; tying your negotiators hands in another thing, Mr. Chairman, and we may have some debate as to what the word "consultation" means. . . . Certainly we should have discussion about our objectives and what our basic policy is and what we would try to achieve; but when one begins to rigidify

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session, January 13 1987, 40.

[65]Ibid., 51.

[66]Ibid., 66.

[67]Ibid. Steven Dryden, in *Trade Warriors*, echoes these comments in his analysis of the evolution of the USTR's role in American trade policy. According to Dryden, Robert Strauss's tenure as STR during the Carter Administration represented a high point in the Office's influence over trade policy followed by approximately five critical years of drift until the appointment of Clayton Yeutter in 1985.

> that process, it can really turn out to be counter productive.[68]

In most other principal-agent relationships, it is hard to imagine the agent splitting hairs over the precise interpretation of consultation. In most principal-agent relationships, the principal is often the agent's employer. Were a company experiencing losses due to inefficient distribution of its resources, it might consider restructuring its operations. In a similar fashion, Congress as the principal in the American trade policy process was revisiting restructuring plans of its own. Senator William V. Roth (R-Delaware) wondered openly whether or not the Executive branch could be better organized to promote U.S. trade interests. "You [Ambassador Yeutter] and your office have responsibility for negotiation, but the administration and the collection of data and information is a matter for the Department of Commerce. That makes for conflict."[69] Although Ambassador Yeutter had few complaints about the current structure of trade policy-making, and did not believe responsibility for trade could be narrowed down to a small number of individuals or one department, Senator Roth disagreed.

> My concern is that, for example in this Administration, and it has not been too unlike what has happened in the past, it took several years for it to sort out exactly who was responsible for what, and there have been great turf wars, and I don't think this has helped the trade picture.[70]

Clayton Yeutter did his best to defend Administration trade activities in front of the Finance Committee, but may have inadvertently given the Senators one of the best arguments for restructuring the institutions that set U.S. policy. In a particularly heated exchange between Yeutter and Nelson Rockefeller (D-West Virginia) over Administration

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[68]See U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st session, February 19, 1987, 104.

[69]Ibid., 106.

[70]Ibid., 107.

inaction on several issues, Yeutter shot back

> It is a different situation than it was when Bob Strauss was here. Bob is a dear friend, and I am a great admirer of him and I think he was an outstanding USTR. But we have five times as many issues on our plate today as Bob had when he was U.S. Trade Representative– five times. Now the President of the United States cannot get involved in all of those issues. We have got dozens of balls in the air, and it is just impossible unless he is going to devote all of his time to trade matters. You have got to delegate in government; you can't do everything yourself. We can't expect the President of the United States to make trade policy decisions in 50 different areas.[71]

The Senate Finance Committee report that followed echoed many of the complaints voiced during the hearings. Among the conclusions the Finance Committee charged that existing procedures had been significantly undermined, allowing foreign countries to take advantage of divisions within the American system. Congressional consultation had deteriorated and "the interagency process led by the Office of the USTR for formulating policies on trade to recommend to the President has been alternately discarded, avoided, and undercut."[72] In other words, a weak USTR, an Administration ambivalent toward trade issues, diffuse lines of responsibility within the Executive, and an extraordinarily heavy workload brought about by increasingly complex economic conditions necessitated a change of approach for American policy-makers.

The Office of the USTR had only periodically functioned well enough to remedy transparency as one of the key agency problems between Congress and the Executive. In 1962, responsibility for trade policy was removed from the foreign policy oriented State Department and given to the USTR. In doing so, the principal intended to both encourage and restrict the activities of its agent. In 1962, Congress could have resumed control of trade policy, but instead left responsibility for trade in the hands of the Executive where it

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[71]Ibid., 110-11.

[72]U.S. Congress, Senate, Committee on Finance, *Omnibus Trade Act of 1987, Report of the Committee on Finance, United States Senate on S. 490 Together with Additional Views*, 100th Congress, 1st session, June 12, 1987, 5-6.

had been since 1934. At the same time, Congress increased its oversight capacity of its agent's activities by creating a new office with specific responsibilities. However, by the late-1980s the uneven results of these institutional changes and the challenges of globalized trade required further alteration in the principal-agent relationship. Did this mean scrapping the USTR? Would Congress reassert its Constitutional prerogatives over foreign commerce as in the days before Smoot-Hawley?

Economic theory suggests that neither outcome was likely. The relationship between principal and agent implies a reciprocal need for each other in order to maximize their respective welfare. Even modern mail-order companies such as Dell Computer need sales representatives, shipping companies, and advertisers as agents in order to conduct an efficient business. As long as the arrangement remains effective for both parties, little needs to be changed. However, when it becomes ineffective for capturing the desired gains from trade, restructuring becomes necessary. The Congressional relationship with the Executive is similar. Between 1986 and 1988, Congress began the process of altering what it perceived to be its ineffective working relationship with the Executive. Although this period has commonly been assessed as being part of a period of Congressional dominance over trade issues because of the intense partisan bickering at and between both ends of Pennsylvania Avenue, the evidence supports a more benign restructuring of the principal-agent relationship that reflects its reciprocal and interdependent nature.

CHAPTER 5

OMNIBUS LEGISLATION 1986-1988

Throughout the 1970s and early 1980s, the United States' economy seemed to be in permanent crisis mode. The high unemployment rates and negative economic growth of the early 1980s seemed to flow seamlessly out of the oil crisis and stagflation plagued 1970s. Unemployment statistics from 1982 were but one sign of a much grimmer economic picture. While the official unemployment rate was 9.7% for 1982, the actual rate was thought to be much higher because official statistics did not account for the many who were thought to have simply dropped out of the job market altogether. Economic expectations were so low in this period that when in 1984 the unemployment rate improved to an anemic 7.5%, Ronald Reagan, on his way to a landslide reelection victory, could claim it as evidence that it was "Morning Again in America."[73]

During the Reagan years, the Administration, and Reagan in particular, repeated the oft heard arguments by postwar economic planners in favor of an open, liberal world economic system.[74] Speeches extolling the virtues of open economies were almost always coupled with dire warnings of the costs associated with a return to the nationalistic,

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[73]See United States Bureau of the Census, *Statistical Abstract of the United States: 1996* (116th edition) (Washington, D.C.: GPO, 1996), 393. See Lou Cannon, *President Reagan, The Role of a Lifetime* (New York: Simon and Schuster, 1991) 232-3; Destler, *American Trade Politics*, 55-6; 7.5% unemployment to gain political points in 1984 is particularly striking given late 1990s unemployment rates which have consistently hovered at or below 5%.

[74]See, U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: U.S. Government Printing Office, 1986), Ronald Reagan, 1986, 506, 624, 651, 658-59, 1302-03.

inward looking economic policies of the inter-war years. However, appeals to the ghost of Smoot-Hawley were increasingly falling upon deaf Congressional ears during the mid-1980s as ballooning budget and trade deficits, coupled with discouraging unemployment statistics focused Congressional attention on economic issues.[75] To Democrats, as well as a growing number of Republicans, the Reagan Administration had been too passive on trade related economic issues. Reagan's unwavering belief in the merits of unfettered trade in the face of these problems struck members of his own party as being indifferent to the needs of their constituents.[76] The President's attempts to quell Congressional and public criticism were ineffectual.[77] The Administration's public pronouncements of a new get tough approach with unfair foreign trade practices and token moves toward reducing the U.S. trade deficit were largely seen as efforts to undercut Congressional momentum on trade issues.[78]

Congressional activism in trade was by no means limited to complaining about the Administration. We have already seen how dissatisfaction with the inconsistent operation of the USTR's Office within the Executive branch prompted proposals to once again alter the agent's relationship with the principal. Beginning in late 1985, with the trade deficit projected to top $160 billion, both houses of Congress began considering measures to alter the American trade picture. When finally passed by both Houses in 1988, the Omnibus Trade and Competitiveness Act, at more than one thousand pages, became the longest, and most comprehensive piece of trade legislation in the postwar era.[79] It also

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[75]*Congressional Quarterly Almanac*, 1985 ed. (Washington, D.C.: Congressional Quarterly Inc., 1985) 253-4.

[76]Ibid.

[77]See "Remarks at White House Meeting with Business and Trade Leaders," September 23, 1985, in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: U.S. Government Printing Office, 1985), Ronald Reagan, 1985, 1127-29; *New York Times*, September 24, 1985, D26.

[78]See *New York Times*, September 24, 1985, D26 and April 1, 1986, D1.

[79]Destler, *American Trade Politics*, 96.

marked the first time since before Smoot-Hawley that the House of Representatives had initiated trade legislation of any kind.[80] The most common interpretation of this period is rooted in a mixture of bureaucratic politics and Congressional behavior models of policy processes. They generally conclude that the Omnibus Act was the result of a period of Congressional ascendancy over the Executive on trade issues. Whereas the outward looking foreign policy Executive initiates economic policy in the national interest, the Legislative branch is viewed as the inward looking, protectionist wing of government whose primary interest is in catering to the narrow interests of constituents.[81] Coupled with the rancorous debate over trade that took place in this period, the various proposals being considered by Congress for its Omnibus legislation in early 1986 are strong evidence of an ascendant, protectionist Congress.[82] Although these events could be interpreted as a Congressional victory over the Executive in its efforts to win back control over authority ceded to the Executive in 1934, a closer examination yields a different conclusion.

Throughout 1986, House Democrats were using their majorities on key committees to promote individual pieces of trade legislation that would eventually become part of House Resolution 4800. Six key committees -- Ways and Means, Foreign Affairs, Energy and Commerce, Education and Labor, Agriculture, and Banking, Finance and Urban Affairs -- all had significant roles in creating the massive Omnibus bill that was

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[80]*Congressional Quarterly Almanac*, 1986 ed., 339-441; Destler, *American Trade Politics*, 92-96.

[81]See Pastor, *Congress and the Politics*, 31-42.

[82]Many foreign governments have mistakenly adopted the simple view of Congress that it is an inherently protectionist institution and to be avoided if at all possible. See for example *House of Commons Debates*, 33rd Parliament, 1st session, Vol 5, 1985, September 26, 1985 (Ottawa: Supply and Services Canada, 1985), 7058. In fact, one of Canada's foremost goals in pursuing the American talks was to secure assured access to the American market and some measure of immunity from contingency protection laws which Canada felt Congress was increasingly disposed toward using to solve trade disputes. See Michael Hart, *Decision at Midnight: Inside the Canada-U.S. Free Trade Negotiations* (Vancouver: UBC Press, 1994), 42, 93-98, 107-110.

eventually approved by the House on May 22, 1986, by a wide, bipartisan margin of 295-115. Condemnation of the House bill from the Administration was swift and categorical. Deputy Press Secretary Larry Speakes charged that the bill's "meat-axe approach" to trade was a reversion to the worst days of Smoot-Hawley that would destroy any potential gains from a new round of multilateral GATT negotiations.[83] Much to the delight of the Administration, H.R. 4800 died when the ninety-ninth Congress recessed for November mid-term elections and before the Republican controlled Senate could act on concurrent legislation. Unfortunately for the Administration, when the 100th Congress convened in January 1987, trade was again the number one issue. The difference in 1987 was that the outcome of mid-term elections gave Democrats in the new Congress a majority in both Houses.[84]

The Senate Finance Committee, chaired by Lloyd Bentsen (D-Texas), wasted little time addressing trade issues when he convened hearings on the subject on January 13. Bentsen opened the hearings himself by saying that the purpose of the hearings was to "help develop a national consensus on the goals of American trade policy."[85] George Mitchell (D-Maine) expressed the sentiment of most Democrats when he said he was

> pleased that the Chairman has announced trade as the top priority of this Committee and the first item on our agenda this year. . . . Although this committee did not report out a trade bill in the last Congress [referring to the Omnibus Bill], we did invest considerable time and effort in reviewing the various options

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[83]"Statement by Principal Deputy Press Secretary Larry Speakes on House of Representatives Approval of Omnibus Trade Bill," in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: U.S. Government Printing Office, 1986), Ronald Reagan, 1986, 658-59. President Reagan criticized the measure by saying that the bill was the product of protectionist Democratic leadership in the House that sought to close markets, raise barriers, and subject America to retaliation from other countries. See ibid., 650-51.

[84]See *Congressional Quarterly Almanac*, 1986 ed., 341.

[85]Opening Statement by Lloyd Bentsen, Chairman, Finance Committee, in U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st session, January 13, 1987, 2.

> available or amending our trade remedy laws and fashioning an effective trade policy for the nation. All of us are familiar with the issues. I hope we can build upon what we learned last year and move without delay to approve comprehensive trade legislation.[86]

Committee Republicans argued for restraint lest any trade bill enacted by Congress be overly protectionist, but nevertheless acknowledged that a comprehensive trade bill was inevitable.[87] In fact, in August of 1988, after overcoming a veto by President Reagan,[88] the Omnibus Trade and Competitiveness Act of 1988 was formally signed into law. However, what did legislators actually do between 1986-88? Many members of the Reagan Administration worried openly that what Congress proposed would result in a compulsory and draconian approach to international trade. In early 1986, several proposals being put forward lent credence to that position. For example, early committee proposals would have required mandatory, rather than the current practice of discretionary, Presidential retaliation against foreign countries found by the International Trade Commission to be engaging in unfair trade practices. Another proposal would have mandated punitive restrictions on imports from countries that subsidized the extraction of natural resources. Members of Congress also wanted procedures on escape clause petitions relaxed to make it easier for threatened industries to obtain import protection. However, the most egregious proposal, at least as far as the Administration was concerned, was the so-called Gephardt Amendment. In an effort to reduce the trade deficit, the Executive branch would

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[86]See Opening Statement by George Mitchell (D-Maine), in ibid., 4

[87]See Opening Statement by John Danforth (R-Missouri), in ibid., 32; Statement by Bob Packwood (R-Oregon) in U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st session, February 19, 1987, 5.

[88]See *Veto of H.R. 3, Message from the President of the United States Transmitting His Veto of H.R. 3, a Bill to Enhance the Competitiveness of American Industry, and for Other Purposes. May 24, 1988*, in U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st session, February 19, 1987. The primary objection of the Administration was the inclusion of the plant closing notification measure.

have been compelled to engage in negotiations with countries that maintained large trade surpluses with the United States. If negotiated reductions in the trade imbalance could not be reached, the President would then have been required to impose import quotas or raise tariffs in order to reduce deficits by 10% per year.[89]

As momentum built for many of these proposals, particularly after the 1986 midterm elections returned control of both Houses to the Democrats, the Administration went into damage control mode. In February 1987, the Administration dispatched Treasury Secretary James Baker and USTR Clayton Yeutter to testify before Lloyd Bentsen's Senate Finance Committee, hoping to diffuse as many restrictive proposals as possible. As a counter to Congressional motivation, Baker unveiled the Reagan Administration's own competitiveness plan. The President's plan was short on specifics and full of vague references to objectives such as preparing tomorrow's youth through education reform, enhanced research and development, and strengthened safeguards for intellectual property. The President's plan also contained promises to control federal spending but none of these proposals ultimately generated much interest among Members of Congress.[90] However, Baker also included a list of items that the Administration would vigorously oppose, including sector-specific protections, such as import quotas, mandatory retaliation, and limits on Presidential discretion. "Retaliatory proposals," Baker said,

> can be useful in bringing about a solution, but a rigid, statutory mandated approach that dictates to foreign nations is unlikely to lead them to reduce their barriers. It is far more likely to result in a counter attack against United States exports. . . . If we are to be successful in negotiating more open markets, the President really does need the flexibility to bargain. If our negotiators' hands are tied by statutory

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[89]See *Congressional Quarterly Almanac*, 1986 ed., 341-45.

[90]The Senate Finance Committee proceeded primarily on the basis of the provisions in House Resolution 3. See Destler, "U.S. Trade Policy Making in the Eighties," 271; U.S. Congress, House-Senate Conference Committee, *Summary of Conference Agreement on H.R. 3, The Omnibus Trade and Competitiveness Act of 1988*, 101st Congress, 1st session, April 19, 1988.

> mandates to take certain action in specific situations, they can easily be outmaneuvered; or the negotiating process will break down, producing a protectionist result for everyone.[91]

Finance Committee members were apparently not impressed with the President's strategy and launched into some stern criticism of Administration trade policy.[92] Senator Max Baucus (D-Montana) charged that the Administration had been far too confrontational with Congress on trade. "The fact is," he continued,

> that we have this stupendous trade deficit. We are now a net debtor country. All the trend lines are wrong, they are in the wrong direction economically, we have got to get our act together, get our house together, and I am wondering about the degree to which the Administration is truly -- not just lip service -- going to try to deal with the Congress on a less confrontational basis and in a more cooperative tone. I think that some of the mistrust here is due to the confrontation, with this Administration historically labeling so much up here as "protectionism."[93]

Perhaps one of the biggest problems for the Administration in dealing with Congress amicably was the Administration's tendency to interpret any change at all as being some form of protectionism. Administration officials and their Republican allies on Capitol Hill routinely cautioned that protectionism was anathema to an open world trading system.[94]

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[91]Statement of Treasury Secretary James A. Baker III, in U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st session, February 19, 1987, 9 and 41.

[92]See U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st session, February 19, 1987, 42. Senator Max Baucus conceded that while the President's competitiveness proposals were an improvement, they were not nearly enough.

[93]Ibid., 42, 44. Senator Rockefeller (D-West Virginia) likened the rhetoric coming from the White House to a giant Japanese Kabuki dance in which elaborately costumed actors engage in highly stylized and exaggerated acting, singing, and dancing.

[94]See Senator Bob Packwood (R-Oregon) in U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st session, February 19, 1987, 5.

At the same time, members of Congress also spoke from both sides of the aisle in arguing that the world trading system was anything but open. America, they argued, had been the only free trader in the postwar period and it was up to Congress to give U.S. negotiators the tools to force foreigners to play by the same rules.[95] On the surface, Congressional hostility toward the Administration and proposals for dramatically altering the principal-agent relationship might lead to the conclusion that Congress was in a protectionist frame of mind. But is this what Congress really intended? The bipartisan character of Congressional debate during the period and the near consensus among members that something needed to change suggests that Congress may not have been as assertive in this period as commonly portrayed. Although debate between 1986 and 1988 was ostensibly about getting tough on trade, what getting tough on trade would actually entail was subject to vigorous debate.

In addition to the exchange of rhetoric between Congress and the Administration, this period is also remarkable for the level of criticism emanating from both ends of Pennsylvania Avenue directed at the trade practices of foreign countries, particularly Japan. Although Japan was not the only country enjoying large trade surpluses with the United States, because Japan's surplus was the largest it became an easy target for American criticism.[96] Japan, Canada, Brazil, South Korea, and several others may all have

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[95]For Republicans, see Representative Doug Bereuter (R-Nebraska) in U.S. Congress, House, Committee on Foreign Affairs, Subcommittee on International Economic Policy and Trade and on Western Hemisphere Affairs, *United States/Canada Trade Relations, Hearing Before the Subcommittees on International Economic Policy and Trade and on Western Hemisphere Affairs of the Committee on Foreign Affairs*, 99th Congress, 2nd session, August 12, 1986, 23; Representative Carlos J. Moorhead (R-California) in U.S. Congress, House, Committee on the Judiciary, Subcommittee on Courts, Civil Liberties, and the Administration of Justice, *Intellectual Property and Trade– 1987, Oversight Hearings Before the Subcommittee on Courts, Civil Liberties, and the Administration of Justice, of the Committee on the Judiciary*, 100th Congress, 1st session, March 18 & 26, 1987, 6.

[96]The bilateral trade deficit with Japan still attracts the attention of lawmakers. In 1995, for example the bilateral current account deficit with Japan reached nearly $60 billion. Meanwhile, with respect to Canada, America's current account went from a

had trade surpluses with the United States, but were the trade practices of these nations responsible for a $170 billion trade deficit? Because of their increasingly important role in international trade, non-tariff barriers were being addressed on several fronts, including the Uruguay Round of the GATT and bilaterally in the so-called Structural Impediments Initiative launched in 1989 by the United States and Japan. Rhetoric emanating from private industry, Congress, and the Executive, at times verging on xenophobia, belied the fact that considerable evidence existed that American trade woes were largely home grown.[97] United States Trade Representative Clayton Yeutter reminded Congress on several occasions that it was futile to try dealing with a $170 billion deficit through trade legislation or through negotiations. Most economists, he believed, thought that more than ninety percent of America's trade deficit was the result of macroeconomic policies at home and abroad.[98] There were several contributing factors to America's trade deficit such as high interest rates and a strong dollar, but the chief culprit was the huge U.S. budget deficit. As national savings rates declined in the 1980s, the United States increasingly

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modest surplus in 1993 to a nearly $8 billion deficit in 1995. See United States Bureau of the Census, *Statistical Abstract of the United States: 1996* (116th edition) (GPO: Washington, D.C.: 1996), 786.

[97]For examples of criticism of foreign trade practices from the private sector see, U.S. Congress, Joint Economic Committee, Subcommittee on Trade and Productivity, and Economic Growth, *International Piracy Involving Intellectual Property, Hearing Before the Subcommittee on Trade and Productivity, and Economic Growth of the Joint Economic Committee*, 99th Congress, 2nd session, March 31, 1986; U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st session, January 13 and 15, 1987, 137-43, 149-70, 176-88.

[98]U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st session, February 19, 1987, 110. See also Clayton Yeutter in United States Department of State, Office of Public Communication, Bureau of Public Affairs, *Department of State Bulletin* 86 (May 1986), 67-8.; See Robert Strauss Testimony in U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st session, January 13, 1987, 36; Paul Krugman, *The Age of Diminished Expectations* (Cambridge: MIT Press, 1992), Chapters 4 & 7.

relied upon foreign capital to meet budget shortfalls. Since as a matter of straightforward accounting the United States can only spend as much as it sells without a deterioration in its balance of payments position. These factors coupled with American fiscal expenditures, particularly on defense, contributed to the explosion in the current account deficit. Only massive inflows of foreign capital allowed the United States to sustain its spending.

The home grown nature of America's trade problems was driven home by a Congressional Budget Office (CBO) study in June 1987. To those who looked to international trade negotiations such as the Uruguay Round of the GATT to solve America's trade problems, the Budget Office was blunt in suggesting those hopes were misplaced because the major cause of the trade deficit was really the federal budget deficit.[99] The merits of international negotiations, the Budget Office concluded, were from the long term benefits of an open trade regime. According the CBO,

> Governments are increasingly resorting to policies that are not regulated by GATT, and that conflict with its principles of open and nondiscriminating trade. . . . As tensions rise, this tendency may escalate into retaliatory measures and countermeasures. The importance of the Uruguay Round lies not so much in how any one of the items on its agenda is resolved as in the recognition by governments of the need to modernize the GATT framework so as to reflect the increasing importance of international markets, and to accept the resulting changes in their own policies.[100]

As a result, the CBO study also concluded that Congress should provide new negotiating authority for the Uruguay Round along with policy direction for the Executive. Much of the debate during the mid-1980s was centered around how to save mature, or sunset,

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[99]United States Congress, Congressional Budget Office, *The GATT Negotiations and U.S. Trade Policy,* June 1987 (Washington, D.C.: U.S. Government Printing Office, 1987), ix. See also Gerald M. Marks, Director of Department of Commerce in Chicago, in *New York Times*, April 18, 1987, A19 who said "Bashing other countries for economic problems ignores many of the facts about what causes the problem. Reluctance to export, the demand created by our huge trade deficit, and consumers' propensity for buying rather than saving, have caused our huge trade deficit."

[100]Ibid.

industries such as steel and textiles However, the list of threatened industries increasingly began including high-technology industries such as telecommunications and semiconductors.[101] In 1986, another CBO study examined the effects of sheltering domestic industries from import competition. It concluded that

> Trade protection is now mainly intended to increase an industry's international competitiveness. . . . In competitive markets, protection will generally increase prices, profits, output, and employment. In turn, higher profits supposedly provide firms with the resources to make the investments necessary for them to compete more effectively. In the cases considered in this report, however, lack of investment was not the sole -- or even the primary -- source of the industries' competitive difficulties.[102]

Import competition was a significant problem before protection was granted, restraints were ineffective in substantially reducing import competition, and, most significantly, according to the CBO import restraints had "not substantially improved the ability of domestic firms to compete with foreign producers."[103]

Evidence that suggests little could be done about America's trade deficits until budget deficits were taken care of, and the CBO's own recommendation that new negotiating authority be granted to engage in GATT negotiations both seem at variance with much of the rhetoric of the period and many of the proposals for Congressional trade

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[101]See U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st session, February 19, 1987, 110-11. See also Laura D'Andrea Tyson, *Who's Bashing Whom?: Trade Conflict in High Technology Industries* (Washington, D.C.: Institute for International Economics, 1992).

[102]United States Congress, Congressional Budget Office, *Has Trade Protection Revitalized Domestic Industries?*, November 1986 (Washington, D.C.:, Government Printing Office, 1986), 97.

[103]Ibid. However, proponents of temporary relief point to success stories such as the recovery of Harley Davidson Motorcycle and the U.S. steel industry as examples of industries that managed to rebuild their competitiveness after being granted temporary import protection.

legislation in the 1980s. Congress may have been unhappy with the way the Administration was handling trade policy, but as the evidence suggests, Congress was not about to reassert control over trade policy as in the days before Smoot-Hawley, nor was Congress about to force a narrow, protectionist agenda upon the Executive branch that would surely have negative consequences for the multilateral trade system. In spite of America's battles with its trading partners, the overwhelming evidence still supported a liberalized trade regime. In fact, the final outcome of the 1988 Omnibus Trade and Competitiveness Act demonstrates that depicting Congressional-Executive interaction over trade as an adversarial, zero-sum relationship oversimplifies each body's position in the trade policy-making process. The final result demonstrates that Congress sought not to punish its agent for bad behavior or even eliminate the agent altogether, but rather to alter the institutions that its agent had at its disposal in the conduct of trade policy in a changing and increasingly competitive international economy. As suggested by agency, Congress altered institutional arrangements in 1988 by creating incentives and procedures that both constrained and created incentives for the agent in a low cost way to ensure more effective outcomes.

The most obvious piece of evidence suggesting a more cooperative result than commonly depicted was the bipartisan and overwhelming vote in favor of the Omnibus package in both Houses; 376-45 in the House, and 85-11 in the Senate.[104] More important, however, were the final provisions of the legislation. The most egregious proposals, such as the Gephardt Amendment mandating reductions in U.S. bilateral trade deficits with specific countries, and the plant closing notice, were eliminated from the final bill, while others, such as mandatory retaliation and investigations, were altered to make them less draconian.[105] However, there were important institutional changes in five key areas:

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[104]*Congressional Quarterly Almanac*, 1988 ed., 209.

[105]The plant closing provision was eliminated at the insistence of the White House, but later passed by Congress as a separate piece of legislation, Senate Resolution 2527, on August 4, 1988 (PL 100-379).

1) The Omnibus Bill required the President's annual report to Congress on trade agreements to include a policy agenda and expanded the role of private-sector advisory committees which consult with the Executive on broad aspects of trade policy as well as on specific trade issues.[106]

2) The Omnibus Bill designated the United States Trade Representative as having primary responsibility for developing, coordinating, and implementing international trade policy and was to be the principal spokesperson and negotiator for American interests in international trade. Coupled with this responsibility, the USTR was also required to continually consult with the House Ways and Means and Senate Finance Committees on the progress of overall trade policy as well as specific actions under trade laws.

3) The Omnibus Bill transferred from the President to the USTR authority to identify and investigate unfair foreign trade practices. Discretionary authority was also transferred to the USTR to decide the most appropriate actions to take against unfair determinations. Time constraints on investigations and punitive action following positive determinations were also imposed.

4) Section 1342 of the Omnibus Act amended the Section 337 of the Tariff Act of 1930 (Smoot-Hawley) by relaxing the criteria under which U.S. intellectual property right holders could obtain relief from the imports of countries that did not adequately protect U.S. intellectual property rights.[107] Furthermore, it offered protection for infant industries

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[106]See U.S. Congress, Senate, Committee on Finance, *Omnibus Trade Act of 1987, Report of the Committee on Finance, on S. 490 Together with Additional Views*, 100th Congress, 1st session, June 12, 1987, 5-6.

[107]See Testimony of Ralph Oman, Register of Copyrights and Assistant Librarian for Copyright Services in U.S. Congress, House, Committee on the Judiciary, Subcommittee on Courts, Intellectual Property, and the Administration of Justice, *Intellectual Property, Domestic Productivity and Trade, Hearing Before the*

by stipulating that if a U.S. industry "exists or is in the process of being established," it is unlawful to import or sell within the U.S. articles that infringe a valid U.S. copyright, patent or are made by processes covered by a valid U.S. patent.[108]

5) Finally, the heart of the Omnibus Act amended section 301 of the Trade Act of 1974 to require the USTR to identify and draft target lists of countries who engage in unfair trade practices. Also known as the "Super 301" the USTR was to investigate and determine which practices, if eliminated, would generate the greatest benefit for U.S. exports. Upon determination of unfair trade, the USTR was required to engage specific countries in bilateral talks aimed at eliminating those practices. The new law also called for retaliation equal to the level of injury incurred by U.S. industry resulting from foreign unfair trade practices. Retaliation could be waived, however, if it were shown to be inconsistent with

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Subcommittee on Courts, Intellectual Property, and the Administration of Justice, of the Committee on the Judiciary, 101st Congress, 1st session, July 25, 1989, 103. Under the 1930 Act, firms had to demonstrate that intellectual property right infringement had "the effect or tendency . . . to destroy or substantially injure an industry, efficiently and commercially operated, in the United States." The Omnibus legislation changed "effect or tendency," to "threat or effect" and no longer required that the firm demonstrate its own efficient operation. See also Judith Goldstein, "Ideas, Institutions, and American Trade Policy,"188-197. Section 337 should not be confused with the more common usage of "escape clause" in the literature. The more common form refers to exemptions for uncompetitive industries hurt by increased imports of goods affected by reductions in U.S. tariff rates. Originally codified through Executive Order 9381 by President Truman in 1948, this U.S. backed principle also became Article XIX of the GATT. Like Section 337, successive revisions of escape clause language have altered industry ability to obtain relief. Unlike 337, however, revisions of escape clause language have actually made it more difficult to obtain relief. See Goldstein, 190.

[108]See U.S. Congress, House, Committee on the Judiciary, Subcommittee on Courts, Intellectual Property, and the Administration of Justice, *Intellectual Property, Domestic Productivity and Trade, Hearing Before the Subcommittee on Courts, Intellectual Property, and the Administration of Justice, of the Committee on the Judiciary*,101st Congress, 1st session, July 25, 1989, 66-70, 106-107. On November 7, 1989, the USTR announced that the GATT Council had ruled Section 337 to be inconsistent with GATT principles, but that the Administration would continue to enforce existing statutes pending revisions to U.S. trade laws.

GATT rules, if offending trade practices were stopped, if retaliation would harm the U.S. economy, or if such action would jeopardize national security.[109]

Were it not for the discretion given to the USTR regarding mandatory retaliation, these proposals could almost universally be interpreted as protectionist.[110] In fact, these particular changes to the agent's relationship with the principal have since been declared by some as illegal and inconsistent with U.S. GATT commitments.[111] More charitable characterizations have referred to Section 301 provisions as a combination of "aggressive unilateralism and selective reciprocity."[112] Under the so-called "Super 301," the United States could unilaterally determine what constituted an unfair trade practice and then "invite" offending countries to the negotiating table to reach a settlement on eliminating its

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[109]*Congressional Quarterly Almanac*, 1988 ed., 209-10; Destler, *American Trade Politics*, 126-7; See also O'Halloran, *Process, Politics*, 107-8.

[110]Flexibility in Super 301 cases lay in the ability of the USTR to rescind designations upon elimination of unfair trading practices, discretion over the exact form of retaliation, and complete waiver if sanctions would adversely affect either the national economy or national security.

[111]See *Thirty-first Meeting of the Canada-United States Interparliamentary Group, 1990 Report by the Chairman of the House of Representatives Delegation* (Rep. Sam Gejdenson, Connecticut), 101st Congress, 2nd session, February 22-26, 9-10.

[112]D'Andrea Tyson, *Who's Bashing Whom?*, 257-8, 263. However, U.S. aggressiveness the use of market opening mechanisms was not without historical precedent. Under the provisions of the McKinley Tariff of 1890, the President was authorized to impose punitive tariffs on foreign products that effectively shut them out of the American marketplace as a means of encouraging foreign countries to conclude reciprocity agreements with the United States. In other words, sanctions were imposed as a means of securing U.S. access to foreign markets. Similarly, section 317 of the 1922 Fordney-McCumber Act provided for retaliatory measures to be used against countries discriminating against U.S. commerce in an effort to persuade them to the bargaining table. In spite of the unilateral aggressiveness of these provisions, the predecessors of Super 301 share much with their modern cousin in that all emphasized the opening of markets rather than the erection of higher U.S. barriers to trade. See Eckes, *Opening America's Market*, 71, 88-90.

trade barriers.[113] That these provisions were not made statutorily mandatory reflects both the input of the Executive in the principal-agent relationship, and the recognition by Congress that overly restrictive and punitive provisions forced upon the agent and other countries would be counter productive because of the threat of retaliation.[114] Interesting examples of the flexibility within Section 301 are the "Special 301" provisions designed specifically to deal with unfair trade practices in intellectual property rights, by then a key part of overall U.S. trade strategy.[115] Under these provisions, the USTR can refrain from designating countries as having lax intellectual property protection if "significant progress" is being made, either in multilateral or bilateral negotiations. In May 1990, the USTR did just this by electing not to identify any priority countries and instead placed eight countries on a "priority watch" list, effectively warning them rather than launching formal

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[113]In the cases of South Korea and Brazil, the threat of being placed on a Super 301 foreign trade practices watch list was enough to persuade them into altering their practices almost immediately. See Destler, *American Trade Politics*, 132-33.

[114]Several Administration officials testified before Congress regarding the negative consequences of self-initiating Section 301 cases, or cases where flexibility was severely limited. See Secretary of the Treasury James Baker's testimony in U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st session, February 19, 1987, 41; USTR Carla Hills Testimony in U.S. Congress, House, Committee on the Judiciary, Subcommittee on Courts, Intellectual Property, and the Administration of Justice, *Intellectual Property, Domestic Productivity and Trade, Hearing Before the Subcommittee on Courts, Intellectual Property, and the Administration of Justice, of the Committee on the Judiciary*, 101st Congress, 1st session, July 25, 1989, 57-58.

[115]See Testimony of Ralph Oman, Register of Copyrights and Assistant Librarian for Copyright Services, in U.S. Congress, House, Committee on the Judiciary, Subcommittee on Courts, Intellectual Property, and the Administration of Justice, *Intellectual Property, Domestic Productivity and Trade, Hearing Before the Subcommittee on Courts, Intellectual Property, and the Administration of Justice, of the Committee on the Judiciary*, 101st Congress, 1st session, July 25, 1989, 66-67; "Remarks at White House Meeting with Business and Trade Leaders," September 23, 1985, in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: U.S. Government Printing Office, 1985), Ronald Reagan, 1985, 1127-29.

investigations.[116]

The most important changes to the principal-agent relationship, however, were in the significant transfer of authority away from the President to the USTR. While statutory authority remained in the Executive branch and lines of authority over trade policy and implementation were clarified, these changes also made the USTR itself more accountable to Congress than ever while also making the Executive branch as a whole more accountable than when authority resided exclusively with the President or with the State Department.[117] Although the USTR had always reported often to Congress on trade issues, the oversight capacity of Congress was dramatically enhanced through both the investigatory and consultation responsibilities shifted to and strengthened in the Office of the USTR.

Proponents of Congressional dominance theses or of inter-branch politics models could look at the foregoing and easily conclude that the harsher provisions within the Omnibus Act were a product of Congressional dissatisfaction with the Administration and of increasing strength and activism on trade issues, particularly under conditions of divided government as existed when Democrats regained control of both Houses in 1986. Bureaucratic politics models might argue that the elimination of the harshest provisions, such as the Gephardt Amendment, and the weakening of others, such as mandatory

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[116]Testimony of USTR Carla A. Hills, in U.S. Congress, House, Committee on the Judiciary, Subcommittee on Courts, Intellectual Property, and the Administration of Justice *Intellectual Property, Domestic Productivity and Trade, Hearing Before the Subcommittee on Courts, Intellectual Property, and the Administration of Justice, of the Committee on the Judiciary*, 101st Congress, 1st session, July 25, 1989, 27-29.

[117]The decision making-process remained diffuse however. USTR was given responsibility for overall coordination and development of policy, but agencies such as the Departments of Commerce, Agriculture and the International Trade Commission contributed to the policy formation and monitoring processes. See U.S. Congress, House, Committee on the Judiciary, Subcommittee on Courts, Intellectual Property, and the Administration of Justice, *Intellectual Property, Domestic Productivity and Trade, Hearing Before the Subcommittee on Courts, Intellectual Property, and the Administration of Justice, of the Committee on the Judiciary*, 101st Congress, 1st session, July 25, 1989, 27.

retaliation, were the product of powerful Executive branch lobbying efforts and compromise between itself and Congress. However, agency is a more effective foreign economic policy lens because it provides a rationale for why harsh agent restrictions were originally considered at all, why the restrictions were weakened, and, most importantly, why the principal also extended and strengthened the agent's mandate in a political atmosphere that could have justified stripping that authority.

One of the reasons that a principal even has an agent, and one of the reasons that a principal-agent relationship continued after the Omnibus Act, is that it fulfils a basic, practical need. The Hudson's Bay Company required agents to help manage its operations across vast distances. In the case of Congress, agents are required because of the impracticality of foreign countries negotiating with a body whose membership consists of the conflicting interests of more than five hundred representatives. In June 1987, the Senate Finance Committee report on the Omnibus proposals acknowledged that "as a practical matter, without some Congressional authority to negotiate, the President will be unable to negotiate successfully on trade."[118] The report continued,

> Governments of other countries realize that under the unique form of government prescribed by the U.S. Constitution, trade agreements cannot be implemented without action of Congress. The President will be a more effective negotiator to the extent he can assure foreign governments that he is implementing a Congressional directive, since the Congress is more likely to approve action in accordance with what it has directed than action it had no part in formulating.[119]

Unfortunately, these words imply an ambivalence on the part of Congress that does not capture the extent to which Congress also depends on the agent where trade policy is concerned. The need for Congress to continue delegating authority to the Executive was captured best by former USTR Robert Strauss in 1987 Senate Finance Committee

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[118]See U.S. Congress, Senate, Committee on Finance, *Omnibus Trade Act of 1987, Report of the Committee on Finance, on S. 490 Together with Additional Views*, 100th Congress, 1st session, June 12, 1987, 5.

[119]Ibid.

hearings when he said

> On a scale of 1 to 10, it is a 10. There is no question in my mind that it [an extension of fast track negotiating authority] must be passed if you hope to have a successful negotiation. And if I represented the Europeans, the Japanese, or others, and you did not have fast track legislation, I would say this negotiation really means nothing. They [Congress] are going to amend this thing to death when it gets back. It is going to sit awhile, and nothing will happen. And why should I put this on the table and then have it bit on here, and nibbled on there, and torn apart here, and then you come back and insist that I do this, that and the other. I want to know when we shake hands and walk out of this room, that is what your Congress is going to vote up or down on or I won't go.[120]

Without delegation of authority, foreign countries will not come to the negotiating table. By extension, a purely protectionist trade bill that harshly constricted the Executive would have achieved the same result. With limited authority to negotiate, there would have been few foreign takers. Significant evidence existed in this period, including the CBO studies, that could have lead legislators to conclude that punitive restrictions on Executive discretion over trade policy would neither improve the trade deficit, nor allow the Executive to conduct negotiations that might net improved trade relations with foreigners. The 1988 Omnibus Trade and Competitiveness Act, ostensibly a protectionist bill from a protectionist Congress, reflected these considerations. As predicted by economic theory, the principal, faced with uncertainty over the trade policy activities of its agent, will seek to create incentives or design institutional procedures that constrain or alter its contractual relationship with its agent in the least costly manner available to ensure the actions taken by the agent yield the desired outcome. We have seen where Congress sought to constrain the agent's activities, but Congress also provided the agent with important incentives.

The incentives designed by Congress in the 1988 Omnibus Act to ensure that the Executive continued to pursue an effective trade policy fall into three basic areas.

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[120]See former USTR Robert Strauss in, U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st session, January 13 and 15, 1987, 53. Specific Fast Track legislation will be addressed in a section to follow.

1) Congress extended, until May 31, 1993, its delegation of authority to the Executive branch to enter and conclude bilateral or multilateral agreements to reduce tariff and non-tariff barriers to trade. The main purpose of the extension was the conclusion of the Uruguay Round of GATT negotiations.[121]

2) As highlighted above, the Omnibus bill strengthened several existing institutions such as the USTR's Office and Section 301 provisions, stopping short of mandating automatic retaliation. Although many of these provisions were branded as "aggressive unilateralism" or "process protectionism," they were in keeping with an overall emphasis in American trade policy in favor of rules based, market opening mechanisms, otherwise known as "fair trade."[122] Collectively, these changes forced the Executive to become more vigilant, some charge more aggressive, in its formulation of trade policy.

3) Perhaps more important than the extension of delegated negotiating authority, Congress also extended until May 31, 1991 so called fast-track authority referred to by Robert Strauss in which negotiated agreements submitted to Congress would be subject to an "up or down" vote but not to amendment. The focus of this extension was also the Uruguay Round of GATT negotiations, which many assumed would near their conclusion in the fall of 1990. However, Congress also provided for the extension of fast-track for an

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[121]President Reagan originally proposed the first ever permanent delegation of negotiating authority from Congress to the Executive, but this motion was never seriously considered. See U.S. Congress, Senate, Committee on Finance, *Omnibus Trade Act of 1987, Report of the Committee on Finance, on S. 490 Together with Additional Views*, 100th Congress, 1st session, June 12, 1987, 4-6.

[122]D'Andrea Tyson, *Who's Bashing Whom?*, 255. American policy in the entire postwar period has consistently preferred rules based trade as opposed to the product specific process that existed before Smoot-Hawley. Exceptions to this have been the acceptance of Voluntary Export Restraint and Voluntary Import Expansion agreements with Japan in Auto and Semiconductor trade in the 1980s that attempted to set specific import/export targets. See also Dryden, *Trade Warriors*, Chapter 13, 318-321 respectively, and footnote 109.

additional two years, until May 31, 1993, unless Congress voted to *disapprove* of such an extension. In other words, it was an automatic extension for two years subject only to a motion to end the authority.[123]

The 1988 Omnibus Trade and Competitiveness Act began in 1985 as a collection of proposals that looked as though they would again concentrate primary responsibility for trade in Congress for the first time since before the Great Depression. At the very least they looked as though they would significantly restrict the Executive's latitude in trade policy. However, in spite of early threats to start a retreat from fifty years of liberal, outward looking trade policies, the final bill ultimately reinforced that liberal, outward-looking position. Although some provisions of the final bill have been attacked as being overly aggressive, those same provisions were changes to the principal-agent relationship that included both incentives and restrictions that forced the agent into a more active, if prescribed, role in the trade policy process. Although provisions such as the so-called Super 301, which mandated the creation of priority country watch lists and required investigations of those countries, were unilateral and somewhat draconian, they were also in keeping with America's oft-heard adherence to a doctrine of free yet "fair"trade.[124] "Fair trade" doctrine, according to Thomas Zeiler, has since the 1960s allowed the United States to praise the virtues of liberalized trade while at the same time appealing to, and to some extend mollifying, domestic protectionist pressures by attempting to force open restricted foreign markets.[125] The Omnibus provisions strengthened some of the tools

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[123]See *Congressional Quarterly Almanac*, 1988 ed., 209-210; see also *Congressional Quarterly Almanac*, 1987 ed., 640-661. A "reverse fast track" provision was also included that operated in much the same way. Congress could at any time pass a motion to rescind fast-track authority if it felt the Executive was not conforming to the mandate of its authority.

[124]See Ronald Reagan, "Remarks at White House Meeting with Business and Trade Leaders," September 23, 1985, in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: U.S. Government Printing Office, 1985), Ronald Reagan, 1985, 1127-29.

[125]Zeiler, *American Trade and Power*, 18-21.

thought necessary to open foreign markets, but stopped short of insisting upon mandatory retaliation. The principal forced its agent into a more aggressive trade posture, but in the end left American trade policy much where it has been throughout the postwar period, liberal and open. The flexibility that remained in the toughest of the new measures preserved this policy position by allowing for workable, if aggressive, solutions to be sought with trading partners.

Concentrating authority in the USTR's Office and strengthening private-sector and Congressional consultation provisions enhanced the principal's monitoring capacity, but also ensured that a broader, less secretive process would lead to greater consensus on trade issues. Dissatisfaction with the secretive approach taken by successive Administrations also led to a transfer of discretionary authority from the President to the USTR. However, given the economic and political atmosphere of the mid-1980s, it is noteworthy, and significant, that discretionary authority remained in the Executive branch at all.

Finally, extending the Executive's negotiating authority for five years was an important vote of confidence by the principal in its agent. However, a more significant indication of that confidence, and the need for an agency relationship, was the extension of fast-track authority. The Omnibus Act extended fast track for three years and provided for an option for two more. The 1991 decision by the Executive to try to exercise that option, to which we now turn, also demonstrates the importance of agency as a foreign economic policy framework.

CHAPTER 6

1991 FAST TRACK EXTENSION

In 1966, U.S. negotiators began international talks aimed at eliminating non-tariff barriers (NTB) to trade. The first such non-tariff barrier to be considered was the American Selling Price (ASP) customs valuation.[126] Because so many non-tariff barriers are intimately tied to domestic laws, negotiating an end to non-tariff barriers, in effect, also implies the elimination, or at least the revision, of domestic laws. With traditional tariff barriers, Congress, under the 1934 RTAA, could pre-set limits on allowable reductions in U.S. tariff rates. Agreements concluded by the Executive under these rules could be simply proclaimed without sending them again to Capitol Hill.[127] However, there was no system of preauthorization where non-tariff barriers were concerned and, therefore, no way to ensure that concluded agreements would become part of U.S. law. When Congress discovered that the Administration was in the midst of negotiations on the ASP, it strenuously objected that the Executive had no authority to negotiate away domestic laws. While the ASP negotiations eventually succeeded, the negotiators failed to win Congressional approval because the terms of the agreement feel outside the limits of statutory tariff reduction authority. To prevent Congress from effectively vetoing future trade agreements, the Nixon Administration in 1973 proposed several changes to the way authority from Congress was delegated to the Executive. The Administration proposed

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[126]Under this method, customs valuation was computed by multiplying the tariff rate not by the price of the imported product, as was standard practice, but by the price (usually a higher price) of the U.S. product with which the import competed. This method usually resulted in a much higher effective rate of protection for domestic industry.

[127]Destler, *American Trade Politics*, 71.

that Congress prescribe in advance the limits of authority to be extended to the Executive, particularly where non-tariff barriers were concerned. In exchange, Congress would stay out of the actual negotiating process, except for informal consultations and progress reports from the Executive, until the final agreement was submitted to Congress for approval.[128] Once submitted, Congress could not amend the agreement and had sixty days in which to submit the agreement to an up or down vote.[129] Enacted in the 1974 Trade Act, these provisions, now known as fast track authority, for the first time in the history of the RTAA program required Congress to take a final look at proposed agreements and pass judgement. Since this change, fast track has become an important pillar of the overall American trade policy process.

On March 1, 1991, President Bush formally requested a two year extension of fast track authority as provided for under the 1988 Omnibus Trade and Competitiveness Act. When Congress originally extended fast track authority in the fall of 1988, the Administration's primary objective was the conclusion of the Uruguay Round of GATT negotiations, the completion of which was then projected to be sometime in late 1990. As a result, the Omnibus Act's original delegation of fast track authority to the end of May 1991 should have been adequate. However, as 1991 began, the GATT negotiations were at a standstill over industrial policies, agricultural trade, and intellectual property rights. In fact, the stalemate over agricultural subsidies proved so difficult that GATT negotiations broke down in December 1990.[130] Nearly five years of negotiations in the Uruguay Round of the GATT had generated nothing but stalemate, and American fast track negotiating

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[128]The President must also notify Congress 90 days in advance of his intent to enter into an agreement.

[129]Pastor, *Congress and the Politics*, 142; Destler, *American Trade Politics*, 71-3.

[130]See George Bush "Remarks and Question and Answer Session of the Economic Club in New York, N.Y.," February 6, 1991, in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: U.S. Government Printing Office, 1991), George Bush, 1991, 120; See also *Public Papers*, Bush, 1990, 703-4; Beth V. Yarbrough and Robert M. Yarbrough, *The World Economy: Trade and Finance*, 3d ed. (Orlando: The Dryden Press, 1994), 424.

authority was only a few months from expiration. Securing a two year extension of fast track authority from Congress was anything but certain. What was the point in prolonging talks that appeared dead? However, by the time President Bush formally submitted his request for fast track extension, the entire focus of the trade debate had shifted. On June 11, 1990, President Bush and President Carlos Salinas de Gortari of Mexico announced plans to pursue a bilateral free trade agreement.[131] Although speculation about the economic potential inherent in a North American free trade zone had been bantered about for years, substantive movement toward such a scenario seemed remote just two months before the Bush-Salinas announcement.[132] In fact, although GATT negotiations were at a standstill, the Bush Administration maintained that multilateral talks were the most important part of America's trade policy and could still be concluded by the end of 1990.[133] Then, on June 27, Bush announced the launch of his Enterprise for the Americas Initiative which had as the ultimate, if somewhat distant, goal, a hemispheric free trade zone.[134]

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[131]"Mexico-United States Joint Statement on Negotiation of a Free Trade Agreement," June 11, 1990, in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: U.S. Government Printing Office, 1990), George Bush, 1990, 806. Formal notification of intent to negotiate with Mexico was not submitted to Congress until September 1990. See Congressional Quarterly Inc., *Congressional Quarterly Almanac*, 1991 ed., 118.

[132]See *New York Times*, November 14, 1979 in which Ronald Reagan announced his candidacy for President in 1980 and called for a 'North American Accord.' See also "Excerpt from Mulroney-Bush News Conference in Toronto," April 10, 1990, in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: U.S. Government Printing Office, 1990), George Bush, 1990, 486; "Interview with Foreign Journalists in the Oval Office," April 16, 1990, in ibid., 507-8.

[133]"Remarks at the Presentation Ceremony for the "E" Star Awards," May 23, 1990, in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: U.S. Government Printing Office, 1990), George Bush, 1990, 703-4.

[134]"Remarks Announcing the Enterprise for the Americas Initiative," June 27, 1990, in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: U.S. Government Printing Office, 1990), George Bush, 1990, 873-77.

When fast track provisions for the Omnibus Trade and Competitiveness Act were being considered, legislators could hardly have envisioned the succession of announcements that dramatically altered the debate over fast track's extension in 1991. Bush's announcements effectively hijacked the debate over trade policy that would otherwise have been focused on the languishing GATT negotiations. Rather than a debate over the merits of extending fast track to resuscitate the Uruguay Round, America's trade relations with the Western Hemisphere, and Mexico in particular, became the central focus.

The 1991 debate over fast track extension clearly highlights several important aspects of the principal-agent relationship in American foreign economic policy and the utility of agency as an economic policy lens. First, the fast track debate demonstrates how the 1988 Omnibus Act altered the institutions that govern how the agent and principal interact. As compared with the late 1980s, the terms of principal-agent interaction were dramatically altered in favor of increased Congressional consultation and oversight of agent activities. Second, the fast track debate demonstrates the reciprocal, cooperative nature of principal-agent relationships. To scholars who view the late 1980s as a period of renewed Congressional activism over trade issues, the fast track debate, superficially at least, looks like a tempting piece of supporting evidence. However, a close look reveals that the relationship between Congress and the Executive is much more reciprocal than at first sight. I. M. Destler, for example, argues that many of the institutions created by Congress, such as the delegation of negotiating authority, the creation of the USTR, and the extension of fast track authority, are evidence that Congress is trying to insulate itself from constituent criticism over trade policy while maintaining its policy influence.[135] In the case of fast track, the up or down vote required on the entire package insulates individual Members of Congress from constituent criticism over specific aspects of concluded agreements while allowing them to vote in favor of trade agreements that promote the national interest. However, arguments such as this cut both ways in that the Executive has

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[135]Destler, "U.S. Trade Policy-Making in the Eighties," 256; Destler, *American Trade Politics*, 14-24.

its own mechanisms, most of them public, for blame shifting. An examination of these issues through the lens of agency reveals that institutional changes to American trade policies are much more of a two way street than is often acknowledged.

When President Bush formally requested the two year extension of fast track authority in March of 1991, extension was by no means a forgone conclusion, in spite of the fact that Omnibus provisions required a *positive disapproval* motion from Congress to prevent an automatic extension. Although the act of passing a *disapproval* motion made fast track extension more likely than if the Omnibus Act had required a *positive approval*, the Bush Administration was taking no chances.[136] Prior to the Mexican and Hemispheric initiatives proposed by the President, the GATT negotiations would likely have been the only matter for consideration, but in March and April of 1991, Mexico had become the major topic for debate and raised some doubt as to the extension of fast track authority. As a result, the Bush Administration launched a two month pressure campaign to win the support of members of Congress for the Administration's initiatives as well as the more immediate goal of fast track extension. While sending Administration officials to Capitol Hill to win approval of Executive initiatives is nothing new, in this case it also demonstrates the reciprocal nature of the principal-agent relationship.[137] The Executive

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[136]For specifics of disapproval methods, see U.S. Congress, House, Committee on Rules, *Disapproving the Extension of Fast-Track Procedures to Bills to Implement Trade Agreements Entered Into After May 31, 1991, Mr. John Joseph Moakley, Chairman the Committee on Rules, Report*, 102nd Congress, 1st session, May 15, 1991.

[137]Pastor, *Congress and the Politics*, 55, quotes the words of a junior Congressman who said "I had heard about lobbyists before I came to Washington and expected to be besieged when I arrived. To my amazement, the first ten lobbyists who came to see me were from the ten Executive departments, offering assistance, literature, and advice on their legislative program." Quoted in "Turning Screws: Winning Votes in Congress," Congressional Quarterly, *Weekly Report*, 24 April 1976, 954. See also Ernest Hollings, in U.S. Congress, Senate, Committee on Finance, *Review of the Uruguay Round: Commitments to Open Foreign Markets, Hearings Before the Committee on Finance*, 102nd Congress, 1st session, April 17-18, 1991, 48. Senator Hollings (R-South Carolina) commented on the heavy pressure exerted by the Administration on Members of Congress during the fast track debate saying, "Well, with regard to consultation, you are right; we are getting it, and that is what really has us, you might say, almost terrorized."

branch was required by the 1988 Omnibus Act to consult regularly with Congress, but by 1991, trade issues were an increasingly important part not only of foreign economic policy, but foreign policy generally.[138] As a result, both the required consultation as well as elective persuasion were becoming important aspects of the principal-agent relationship as the Administration began to rely more heavily on Congress for its ability to conduct foreign policy. While ultimate authority for trade rests with Congress, the Executive, because of delegation and its role as agent, is more familiar with the status and potential of ongoing negotiations. In part because of the additional foreign policy flexibility that discretion over trade permits the Executive, significant incentive exists for the agent to argue in favor of additional flexibility. Since the fast track debate had become ensnared in debate over a Mexican trade agreement, the Administration used its considerable powers of persuasion on the principal in 1991 to gain additional foreign policy leverage.

Neither the principal nor the agent wasted much time in taking up the fast track issue. Just four days after formally requesting the extension, President Bush fired the first salvo in favor of the extension. While he said that the Administration embraced the opportunity to work with the private sector and with Congress on trade issues, the President raised the stakes by echoing a familiar warning to those in Congress who were against the extension.

> And if a disapproval resolution is passed by either House, the Fast Track for all purposes is history; it's gone, as -- I would say with that -- as is our ability to negotiate in the Uruguay Round, the North American free-trade agreement, and the Enterprise for the Americas Initiative. All vital, vital interests of the United States of America. So, a vote against Fast Track is a vote against vibrant

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[138]"This Fast Track authority question is absolutely fundamental to our major foreign policy objectives. And we can't look at it narrowly. We've got to look at it in terms of the big foreign policy picture . . . . It is in the vital national interest of the United States that we get this Fast Track authority." President Bush,"Remarks at a White House Briefing on Fast Track Authority Extension, May 1, 1991, in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: U.S. Government Printing Office, 1991), George Bush, 1991, 457. See also *Public Papers*, Bush, 1990, 873-77, 982-91, 1226-32.

international trade.[139]

Two days later, on March 7, House Ways and Means Committee Chairman Dan Rostenkowski (D-Illinois) and Senate Finance Committee Chairman Lloyd Bentsen (D-Texas) sent the President a letter warning the Administration that fast track extension was not automatic. It was an invitation to the agent to persuade the principal that an extension was in the best interests of the whole country. "You should be aware," Rostenkowski and Bentsen began,

> that this process will not be easy. . . . A number of members of Congress have expressed concern about the proposed extension of fast-track authority, particularly as it applies to the proposed free trade agreement with Mexico. They have identified a number of legitimate concerns that, in our judgement, should be addressed in a meaningful way before the Congress considers the extension of fast track authority. Specific concerns include the disparity between the two countries in the adequacy and enforcement of environmental standards, health and safety standards and worker rights. While we recognize that issues such as these are not typically addressed in a trade agreement, we believe that such issues need to be addressed in this case, either within the agreement itself or through some appropriate alternative context, within the same time frame as the negotiations.
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> The time period for Committee deliberations on the issue of the proposed extension of fast-track procedures expires on May 15. We, therefore, request that you provide us, by May 1, your thoughts on how the Administration intends to address these and other relevant issues. Such an action plan is essential to the Congress as we deliberate on your fast-track request. More importantly, successful implementation of such an action plan is likely to be exceedingly critical when and if that Congress considers approval of any trade agreement which results from the negotiations. Whether such an agreement is ultimately approved by the Congress will depend on an assessment of whether the agreement has a net positive effect on jobs and wages in the United States.[140]

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[139]President Bush, "Remarks at a Briefing on Extension of the Fast Track Trade Negotiation Authority," March 5, 1991, in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: U.S. Government Printing Office, 1991), George Bush, 1991, 212-13.

[140]See letter from Congress (Rostenkowski and Bentsen) to the President, March 7, 1991, in U.S. Congress, Senate, Committee on Finance, *Extension of Fast Track*

While Congress began hearings on fast track, the Administration continued its public campaign to persuade the principal into extending additional authority. In an April 8 speech before business leaders in Houston, Texas, the President again argued that the failure to extend fast track authority would destroy efforts to conclude trade agreements with foreign countries, but with a twist; Bush equated fast track extension with America's ability to promote freedom and prosperity around the globe. " A vote against Fast Track," he said, "is a vote against things that we all hold dear, prosperity at home and growth in other lands."[141] According to Bush, many of the concerns raised by members of Congress were actually reasons to extend fast track.[142] Issues such as labor standards, the environment, and U.S. jobs could all be addressed within negotiations. Given America's prominent role in the global economy, "the vote on fast track [was] really a vote on what kind of America we wanted to build."[143]

Meanwhile, in hearings on Capitol Hill, the Administration faced tough questions on the specific need for extension that at the same time afforded an opportunity for the agent to allay concerns that its proposals would be contrary to the interests of the principal. USTR Carla A. Hills began her Senate Finance Committee testimony by pointing out that trade policy was the product of a genuine partnership between the

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Legislative Procedures, Hearing Before the Committee on Finance, 102nd Congress, 1st session, March 14, 1991, 33; see also Senator Max Baucus (D-Montana) in ibid., 4.

[141]President Bush in "Remarks at a Meeting with Hispanic Business Leaders in Houston, Texas, April 8, 1991 in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: U.S. Government Printing Office, 1991), George Bush, 1991, 346.

[142]See also Statement of Representative Tom Coleman (R-Missouri), in U.S. Congress, House, Committee on Agriculture, *Proposed United States-Mexico Free Trade Agreement and Fast Track Authority, Hearing Before the Committee on Agriculture*, 102nd Congress, 1st session, April 24, 1991, 10. Coleman argued that by negotiating rules based trade agreements, farmers would actually be better off because of the recourse they would have through those agreements to air their disagreements with foreigners.

[143]Ibid., 347.

Executive and Legislative branches and that if the Administration was to have any credibility in international negotiations, it needed fast track authority.[144] In the context of principal-agent relationships, what is the point of having an agent if it cannot act on behalf of the principal? Chairman Bentsen, himself openly supportive of extension, wondered what would happen if fast track was not extended: "Would you proceed in the hopes that what ever the final product you put together would, at the end of the day be approved by Congress?"-- to which Hills replied:

> It would not be me who would give up. My trading partners would not negotiate with me. They demonstrated that in 1974, where before fast track they would not negotiate, we required fast track to get them to come to the bargaining table and you cannot blame them for it.[145]

Responding to a similar question from Senator Bill Bradley (D-New Jersey) Hills added

> I can honestly represent to you that the countries will not negotiate with us. They do not want to negotiate where it is all for nil, where it is just a dress rehearsal for the real thing. And they most assuredly will not give us their bottom line if they know that the real thing is not my negotiation, but a subsequent negotiation with 535 negotiators, each of whom have very real interests in their home districts.[146]

Hills' statements highlight the importance of fast track procedures for both the principal and the agent in the American policy process. The main reason that foreign countries will

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[144]Statement of Carla A. Hills, USTR, in U.S. Congress, Senate, Committee on Finance, *Extension of Fast Track Legislative Procedures, Hearing Before the Committee on Finance*, 102nd Congress, 1st session, March 14, 1991, 9.

[145]Ibid., 10; See Hart, *Decision at Midnight*, 142-51 for discussion of the importance of fast track procedures to Canada in the Canada-U.S. free trade talks 1985-87. Without fast track, talks would have been a "non-starter" from the Canadian point of view.

[146]Carla A. Hills, USTR, in U.S. Congress, Senate, Committee on Finance, *Extension of Fast Track Legislative Procedures, Hearing Before the Committee on Finance*, 102nd Congress, 1st session, March 14, 1991, 25.

not negotiate with the United States stems from the unique division of responsibility within the Constitution described earlier. Unlike the authority of negotiators for foreign governments who have the blessing of their heads of state, and who themselves are often the final authority for national economic policy, such responsibilities in the United States are dispersed among different branches of government. Even in parliamentary democracies, trade representatives speak for the entire government and, assuming the government in power has a majority of seats, can enter into trade agreements with little or no opposition.[147] Fast track provides American negotiators a middle ground position whereby negotiators can negotiate on behalf of the entire country and assure foreigners that agreements reached will not be amended after the fact.[148] With fast track, the Administration argued, the United States could entice countries to come to the bargaining table with their best offers in hand, free of the fear that parochial interests in Congress would later try to attach amendments to the agreement.[149]

As a matter of practical necessity, the maintenance of a liberal, relatively open international trade regime based, as much as possible, on rules and principles must have

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[147]Michael Hart offers a view of foreign frustrations over the American division of powers and contrasts them with parliamentary systems in *Decision at Midnight*, 41-42.

[148]See Destler, *American Trade Politics*, 73. It was a middle ground in that while the Administration could promise foreign countries that agreements would not be amended, they could not guarantee that Congress would not reject them.

[149]See Prepared Statement of Carla A. Hills, in U.S. Congress, Senate, Committee on Finance, *Extension of Fast Track Legislative Procedures, Hearing Before the Committee on Finance*, 102nd Congress, 1st session, March 14, 1991, 36; Testimony of Secretary of Agriculture Edward R. Madigan and USTR Carla A. Hills, in U.S. Congress, House, Committee on Agriculture, *Proposed United States-Mexico Free Trade Agreement and Fast Track Authority, Hearing Before the Committee on Agriculture*, 102nd Congress, 1st session, April 24, 1991, 33 and 46; USTR Carla A. Hills Testimony in, U.S. Congress, House, Committee on Agriculture, *Review of Fast Track Extension Request Submitted by the Administration, Hearing Before the Committee on Agriculture*, 102nd Congress, 1st session, March 13, 1991, 16-18; President Bush, "Remarks at a Meeting with Hispanic Business Leaders in Houston, Texas," April 8, 1991, in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: U.S. Government Printing Office, 1991), George Bush, 1991, 345.

some built-in immunity from arbitrary change. The GATT regime has created mechanisms that constrain and discipline the trade policies of member countries.[150] These mechanisms, in effect, serve as reassurance that member states will not be the victim of each other's unilateral actions. Similarly, American fast track authority rules also serve as reassurance to foreign countries that negotiated agreements will enjoy a level of immunity from amendment as they are voted on Congress. Although the Executive needs a basic delegation of authority from Congress to even conduct trade negotiations, that authority alone is rendered meaningless in the absence of fast track. Even if foreign countries agreed to negotiate with Congress on trade issues, it is unlikely that agreement could ever be reached with literally hundreds of mutually exclusive interests all participating. Its concerns over proposed trade agreements with Mexico aside, the members of Congress recognized that the principal also needed the Executive as its agent. In the March 7 letter from Chairmen Rostenkowski and Bentsen to the President that served as both a query into the Administration's approach with Mexico and a warning that Congress holds the ultimate authority, they nevertheless conceded that "the extension of such authority [fast track] is necessary if the Administration is to have any credibility in pursuing negotiations."[151]

The need for an agent to negotiate on trade matters did not, however, prevent critics of fast track extension from trying to stop it. As resolutions disapproving the extension of fast track authority were making their way through both Houses, tough

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[150]See Frank Stone, *Canada, the GATT and the International Trade System*, 2d ed. (Montreal: Institute for Research on Public Policy, 1992), 22-3, and Chapter 4.

[151]See Letter of Rostenkowski and Bentsen to the President, March 7, 1991, in U.S. Congress, Senate, Committee on Finance, *Extension of Fast Track Legislative Procedures, Hearing Before the Committee on Finance*, 102nd Congress, 1st session, March 14, 1991, 33; See also Statement of Senator Lloyd Bentsen, Chair, Senate Finance Committee, in ibid., 2-3; Opening Statement of Senator Lloyd Bentsen, Chair, Senate Finance Committee, in U.S. Congress, Senate, Committee on Finance, *Review of the Uruguay Round: Commitments to Open Foreign Markets, Hearings Before the Committee on Finance*, 102nd Congress, 1st session, April 17-18, 1991, 2-3.

questions continued to be directed at the Administration.[152] In the House of Representatives, Representative Robert Torricelli (D-New Jersey) wondered why Congress would not be in a better position to judge the merits of particular parts of negotiated agreements once they were finalized. While accepting the Administration's point of view that a solid mandate, in the form of delegated authority, was a needed and powerful signal to foreign countries, Torricelli felt that delegating advance authority to the Executive also passed an unacceptable burden onto Congress when the agreement came to them for approval. In his mind, the political pressures on the Members of Congress to approve any agreement would be enormous because of the negative foreign policy message that disapproval would send.[153] Once again, Torricelli argued, American trade policies would ultimately be subordinate to foreign policy considerations. Other members of Congress questioned the need for fast track authority at all, citing examples of other international negotiations, such as arms control, that have needed no additional authority in order to entice foreign countries to either bargain or generate the support of Congress. As part of its strategy, the Administration had consistently emphasized the complexity of

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[152]For procedures used by Congress for disapproval, see U.S. Congress, House, Committee on Rules, *Disapproving the Extension of Fast-Track Procedures to Bills to Implement Trade Agreements Entered into After May 31, 1991, Mr. John Joseph Moakley, Chairman the Committee on Rules, Report*, 102nd Congress, 1st session, May 15, 1991; U.S. Congress, House, Committee on Rules, *Expressing the Sense of the House of Representatives with Respect to the United States Objectives that Should be Achieved in the Negotiation of Future Trade Agreements, Report, Mr. John Joseph Moakley, Chairman the Committee on Rules*, 102nd Congress, 1st session, May 15, 1991.

[153]See Representative Robert G. Torricelli (D-New Jersey), in U.S. Congress, House, Committee on Foreign Affairs, Subcommittees on International Economic Policy and Trade and on Western Hemisphere Affairs, *The North American Free Trade Agreement, Hearings Before the Subcommittees on International Economic Policy and Trade and on Western Hemisphere Affairs of the Committee on Foreign Affairs*, 102nd Congress, 1st session, March 6, 1991, 20-21; U.S. Congress, House, Committee on Rules, *Expressing the Sense of the House of Representatives with Respect to the United States Objectives that Should be Achieved in the Negotiation of Future Trade Agreements, Report*, Mr. John Joseph Moakley, Chairman the Committee on Rules, 102nd Congress, 1st session, May 15, 1991, 2.

trade negotiations and how important it was for American negotiators to have the same negotiating authority as their foreign counterparts. Arms control negotiations were at least as complex at trade talks, and in many respects much more serious, yet significant Executive branch effort had been expended trying to reduce the role of Congress in trade talks through the fast track process. Senator Ernest Hollings (R-South Carolina), appearing before the Finance Committee, noted that although Congress protected its prerogative to amend and submit reservations throughout the arms control negotiation process several important treaties were nevertheless concluded. Therefore, he said:

> If we can do that for our national security, you would expect the same for a little trade treaty. And of course, the plea has always been: Well, wait a minute. If you start trading, then the whole thing will come apart; and they will never come back to the table. We heard that on SALT II. We turned SALT II down, and they were immediately back at the table; and we not only got together an agreement on intermediate nuclear forces, but we ratified that. We live in the real world. We are mature; we are grown; we are good business folks. We are Yankee traders; and if it is in our interest and benefit, we are going to vote for it. And if it is not, we are not going to vote for it. There is no use in having this political nonsense about the complications of it.[154]

Another favorite Administration argument in favor of fast track was that a vote against fast track was a vote in favor of a path towards protectionism and a return to the worst days of the Smoot-Hawley era.[155] By dragging "that old cat across the table," the

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[154]See Senator Ernest F. Hollings (R-South Carolina) in, U.S. Congress, Senate, Committee on Finance, *Review of the Uruguay Round: Commitments to Open Foreign Markets, Hearings Before the Committee on Finance*, 102nd Congress, 1st session, April 17, 1991, 42-43.

[155]See USTR Carla A. Hills in, U.S. Congress, House, Committee on Agriculture, *Review of Fast Track Extension Request Submitted by the Administration, Hearing Before the Committee on Agriculture*, 102nd Congress, 1st session, March 13, 1991, 49; Former USTR William E. Brock in, U.S. Congress, Senate, Committee on Finance, *Review of the Uruguay Round: Commitments to Open Foreign Markets, Hearings Before the Committee on Finance*, 102nd Congress, 1st session, April 17-18, 1991, 52; President Bush, "Remarks at a Meeting of the American Business Conference," April 9, 1991, in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.:

Administration, according to Hollings, was wrongly linking the Great Depression to protectionism.[156] Other Members of Congress questioned acceding to a delegation of negotiating authority for an agreement that had not yet been seen, that Congress would have no part in negotiating, and that was months, perhaps years, away from completion. Adding to the difficulties facing the Members was the lack of credible information on the proposed outcome of the President's new proposals for Mexico and the Enterprise for the America's initiative.[157]

The proposed free trade agreement with Mexico ultimately generated one of the most hotly contested economic debates in America since World War Two. Organized labor, environmental groups, multi-national corporations, academe, and government officials were all intimately involved in the debate. These groups were also well

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Government Printing Office, 1991), George Bush, 1991, 350-51; President Bush, "Remarks at a Meeting with Hispanic Business Leaders in Houston, Texas," April 8, 1991, in ibid., 345-48.

[156]See Senator Hollings in, U.S. Congress, Senate, Committee on Finance, *Review of the Uruguay Round: Commitments to Open Foreign Markets, Hearings Before the Committee on Finance*, 102nd Congress, 1st session, April 17-18, 1991, 44; Several scholars have disputed claims that the Smoot-Hawley bill was a cause of the Great Depression, or that it even exacerbated its severity. See Alfred E. Eckes, *Opening America's Market*, Chapter 4; Paul Krugman, *The Age of Diminished Expectations*, 125-26. It is also interesting to note that no one seriously questioned the Administration's equating disapproval of fast track with protectionism when all that would have resulted was the continuation of the status quo.

[157]Representative Sam Gejdenson (D-Connecticut) in, U.S. Congress, House, Committee on Foreign Affairs, Subcommittees on International Economic Policy and Trade and on Western Hemisphere Affairs, *The North American Free Trade Agreement, Hearings Before the Subcommittees on International Economic Policy and Trade and on Western Hemisphere Affairs of the Committee on Foreign Affairs*, 102nd Congress, 1st session, April 9, 1991, 117. The lack of solid evidence one way or the other did not prevent supporters and detractors alike from claiming, for example, that NAFTA would result in the creation or loss of hundreds of thousands of jobs, depending on which side you accepted. See for example, Paul Krugman, "The Uncomfortable Truth About NAFTA," *Foreign Affairs* 72 (Nov/Dec 1993): 13-19.

represented during debate over fast track extension.[158] In spite of the concerns and objections raised during the debate, the extension of fast track until April of 1993, won comfortable approval from both Houses of Congress. The House Ways and Means Committee and the Senate Finance Committee both reported disapproval resolutions unfavorably out of committee by wide margins that were then reflected in floor votes on the measures.[159] In the final analysis, the defeat of the disapproval resolutions may have been more about the operation of the trade policy institutions that were altered in 1988 than it was about the relative merits of free trade. While the Administration mounted an impressive lobby effort to ensure extension by praising the merits of unfettered markets, closer economic ties in the Americas, and the importance of Mexico as a neighbor, Congress directed the majority of its questions to ensuring that once negotiations began, the agent would be in regular consultations with the principal on the status of the talks. As a result, the Administration expended much of its lobbying efforts reassuring Congress that established procedures would be followed throughout the talks. For example, USTR Carla Hills testified repeatedly in March and April 1991 that fast track extension did not mean that Congress was giving up its ability to influence the progress of trade negotiations. On the contrary,

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[158]See testimony of Stuart Hudson, Acting Director, International Programs, National Wildlife Federation; Professor M. Delal Baer, Senior Fellow and Director, Mexico Project, Center for Strategic and International Studies; Pharis J. Harvey, Executive Director, International Labor Rights Education and Research Fund, all in U.S. Congress, House, Committee on Foreign Affairs, Subcommittees on International Economic Policy and Trade and on Western Hemisphere Affairs, *The North American Free Trade Agreement, Hearings Before the Subcommittees on International Economic Policy and Trade and on Western Hemisphere Affairs of the Committee on Foreign Affairs*, 102nd Congress, 1st session, March 6, April 9 and 16, 1991, 62-86.

[159]The House Ways and Means Committee reported out H Res 101, unfavorably, 9-27. The House then voted 192-231 to reject the measure. The Senate Finance Committee reported S Res 78 unfavorably by a vote of 3-15, while on the Senate floor the motion to disapprove was defeated 36-59. See *Congressional Quarterly Almanac*, 1991 ed., 118.

> As you know well, fast track is neither fast nor a track. In truth, the process is actually quite deliberate. No one is being railroaded into approving agreements that are to be negotiated. Fast track procedures have absolutely nothing to do with the pace at which we conduct our negotiations. While we are eager to capture the benefits that these agreements promise, we will take the time necessary to arrive at agreements that are truly and substantially in the economic interest of the United States. . . . The fast track as perceived by Congress and as implemented by the Executive and by Congress, is a genuine partnership between the two branches. Although only the President can negotiate trade agreements, and fast track's guarantee of timely up or down vote -- at the end of the process is essential to the President's ability to do so -- Congress has a full role throughout the entire process in formulating the negotiating objectives in close consultation as the negotiations proceed.[160]

Furthermore, Hills argued, the high level of Executive-Congressional consultation throughout the proposed talks should result in an agreement and implementing legislation that wins overwhelming approval from Congress.[161] To those who complained that once fast track was extended, Congress was going to be left to vote on an agreement that it had no part in creating, Hills said

> Let me suggest to you that you are not voting for what you have not seen. You do not have to vote for anything. . . . You will have your turn to vote up or down the agreement when you can see it. . . . I invite you to participate in the consultation process, which is constant and heavy with Congress, and then you will see the agreement as it is written. After it is written you can exercise your constitutional prerogative, which is to regulate international commerce by voting for or against the agreement.[162]

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[160]USTR Carla A. Hills testimony in, U.S. Congress, Senate, Committee on Finance, *Extension of Fast Track Legislative Procedures, Hearing Before the Committee on Finance*, 102nd Congress, 1st session, March 14, 1991, 9.

[161]Ibid., 9-10. See also Hills' Prepared Testimony, in ibid., 36. Hills largely repeated these arguments in, U.S. Congress, House, Committee on Agriculture, *Review of Fast Track Extension Request Submitted by the Administration, Hearing Before the Committee on Agriculture*, 102nd Congress, 1st session, March 13, 1991, 16-18.

[162]USTR Carla A. Hills in, U.S. Congress, House, Committee on Agriculture, *Review of Fast Track Extension Request Submitted by the Administration, Hearing Before the Committee on Agriculture*, 102nd Congress, 1st session, March 13, 1991, 49.

The paramount importance of procedural concerns with respect to entering free trade negotiations was further demonstrated in the President's May 1, 1991, response to the March 7 Rostenkowski-Bentsen letter. The President reiterated the power of Congress to vote on any final trade agreements, but emphasized that

> You have my personal commitment to close bipartisan cooperation in the negotiations and beyond. And you have my personal assurance that we will take the time necessary to conclude agreements in which both Congress and the Administration can take pride.[163]

In September 1992, the White House issued a "report card" on the status of the commitments made by the President in his May 1, 1991 response. In it, the Administration outlined the extent of its Congressional and private sector consultations with respect to the NAFTA process, and quoted House Ways and Means Committee Chair Dan Rostenkowski who observed that the "USTR has been relentless in keeping Congress informed and that Congress 'cannot fault the Administration for secrecy.'"[164]

When Congress was considering the 1988 Omnibus legislation, it constrained its agent, but in a way that left significant discretion in the hands of the Executive to conduct foreign trade policy. Fast track represented yet another opportunity to further constrict the agent. Although trade liberalization as a basic doctrine of American foreign economic policy had prevailed for more than fifty years, enough skepticism and uncertainty over free trade with Mexico existed for Congress to have legitimately blocked the extension of fast track. However, like the 1988 Omnibus Act itself, the extension debate was really more

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[163]President Bush, "Letter to Congressional Leaders on Fast Track Authority Extension and the North American Free Trade Agreement," May 1, 1991, in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: Government Printing Office, 1991), George Bush, 1991, 450-51.

[164]*Report of the Administration on The North American Free Trade Agreement and Actions Taken in Fulfillment of the May 1, 1991 Commitments*. Issued September 18, 1992, 65-68. US GPO FEB 93-5908.

about procedural issues and the operation of trade policy institutions than the specifics of America's trade relations with other countries. While the debate over fast track was, at times, as highly contentious as that during the 1988 Omnibus process, fast track, like Omnibus, again highlighted the cooperative nature of the trade policy process. The interests of the principal were not going to be served by severely restricting the activities of the agent in 1991. Given the added difficulties associated with passing *disapproval* motions as opposed to *approval* motions, law makers in 1988 may never have envisioned actually denying fast track extension in 1991. As Chairman Bentsen of the Senate Finance Committee explained, while the President needed authority to negotiate trade agreements, the 1988 Act had built in a number of safeguards into the process, including the fast track extension provision.[165] In 1988, President Reagan had actually requested the first ever permanent extension of fast track authority, but was denied in favor of a two year option, which, Bentsen explained, was designed

> to ensure that Congress was really involved and were well consulted during the negotiations; to ensure that the Administration's eyes did not just glaze over when we expressed the concerns of our constituencies; to ensure that they were really tuned in and listening.[166]

This may be the most important aspect of the 1991 fast track debate. The Omnibus Act had not created institutions that made it easy for the principal to severely restrict its agent, but were designed rather only to monitor its activities. Fast track extension was not a foregone conclusion, but the procedures followed suggest that the principal had in mind a "waiting period" of sorts where both the principal and its agent would reevaluate each other's positions and the potential of existing trade policy institutions for dealing with them.

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[165]See Senator Lloyd Bentsen, in U.S. Congress, Senate, Committee on Finance, *Extension of Fast Track Legislative Procedures, Hearing Before the Committee on Finance*, 102nd Congress, 1st session, March 14, 1991, 2.

[166]Ibid.

Lest one conclude that the Administration's arguments for and Congressional arguments against fast track implies that it is a one dimensional institution that provides the Executive with the lion's share of benefits by giving it freer reign over trade and therefore foreign policy generally, fast track also acts as an important Executive institutional constraint. In many ways, fast track, even if extended liberally and for long periods of time, is at once both an institutional carrot and stick. The incentive within fast track lies in granting the Administration authority to freely conduct negotiations with foreign countries that might otherwise not be willing to negotiate with the more than four-hundred members of Congress. Fast track, by extension, then also represents an important foreign policy tool coveted by the Executive. The stick rests in the additional opportunities the fast track process presents the principal to evaluate, and if necessary rescind, grants of Congressional authority. In addition to the broad delegated authority given to the Executive in extensions of the RTAA program, fast track provides yet another point of contact for consultation with the agent. Finally, although the Executive gets an additional foreign policy tool for its repertoire, Congress by voting up or down at the end of the negotiating process has an opportunity to exercise veto power over agent activities.

A product of the 1988 Omnibus Act, the 1991 fast track extension debate demonstrated how institutional changes in the principal-agent relationship resulted, in some respects mandated, the Executive adopt an open and highly consultative process as Congress considered both free trade with its North American neighbors and the Enterprise for the Americas Initiative. The 1991 fast track debate also demonstrated that the trade policy process is less a product of adversarial inter-branch competition for control over trade policy than it is a mutually beneficial, necessary, and cooperative formulation effort on the part of principal and agent that results in an institutional structure full of both incentives and constraints amenable to both the principal and agent alike. While both the fast track and Omnibus debates focused on detailing the future of the principal-agent relationship in American trade policy, the two major trade agreements concluded in this period present contrasting portraits of principal-agent interaction that the detailing was designed to affect.

CHAPTER 7

THE U.S.-CANADA FREE TRADE AGREEMENT AND THE NORTH AMERICAN FREE TRADE AGREEMENT

In the period under study here, the United States was involved in several international trade initiatives including the Uruguay Round of GATT negotiations and the Enterprise for the America's initiative. During this period, the United States also concluded talks in two of its most important trade initiatives of the postwar period; the U.S.-Canada Free Trade Agreement (FTA) in October 1987 and the North American Free Trade Agreement (NAFTA) in August 1992. Although important differences existed between these sets of talks that make comparison difficult, some of those differences also clearly demonstrate the extent of the institutional change that took place in the American policy process during this period in which the principal-agent relationship between Congress and the Executive was altered and refocused such that the paths taken in concluding both NAFTA and the FTA differed significantly.

There are several factors that set these two sets of negotiations apart from one another and make comparison difficult. First, there is little disputing that NAFTA talks generated significantly more public interest and debate in the United States than did the FTA negotiations. Part of the reason for this disparity in interest stems from the relative importance of each set of talks to the United States. Although liberalizing trade with Canada was not unimportant to the United States, much of the two-way trade between the two countries already enjoyed low tariffs, and American producers stood to gain only modest additional benefits from freer trade with a market of only 30 million people. Canadians, however, heatedly debated the merits of a closer economic relationship with the United States, and the Canadian federal election in 1988 was fought largely on that

one issue. Canadian nationalists bemoaned the loss of sovereignty they associated with the fact that nearly 75% of Canada's exports and 70% of its imports were already dependant on the American market. Contrast this with American figures which show only 18% of American imports and 23% of American exports dependant on the Canadian market, and the reason for the contrasting levels of interest in the FTA in each country is apparent.[167] Compared with U.S. public interest in the FTA debate, the NAFTA debate much more readily captured public attention for several reasons. First, the sheer scale of the proposed free trade zone was impressive as it covered more than $6 trillion in goods and services. Second, the proposed agreement also generated controversy among environmental and labor groups because they feared a loss of jobs and a degradation of standards as two developed nations meshed their economies with that of a developing nation. Third, forces on both sides of the debate pointed to the persistent problem of illegal immigration and claimed that NAFTA would either exacerbate the problem, or help control it via NAFTA-related Mexican economic growth that would act as a disincentive to northward migration. Finally, NAFTA took on increased importance in American foreign policy when it became a major part of the Bush Administration's overall foreign policy agenda during the 1992 general election campaign.

However, these obvious points of difference were not the only reasons for the contrast in American interest in the two sets of talks. Each set of talks is also highly indicative of the contrasting approaches taken by the United States during the negotiating process. Both sets are illustrative of the institutional changes that took place in the period, particularly those initiated by the 1988 Omnibus Trade and Competitiveness Act.

In early August of 1986, before the House Subcommittees on International

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[167]United Nations, Economic Commission for Europe, "The Free Trade Agreement Between Canada and the United States,"*Economic Bulletin for Europe*, Vol 42/90, 1990, 117; For more contemporary figures see United States Bureau of the Census, *Statistical Abstract of the United States: 1996* (116th edition) (Washington, D.C., 1996), 801; Statistics Canada, *Canadian Statistics- Imports and Exports of Goods on a Balance of Payments Basis*, at http://www.statcan.ca/english/Pgdb/Economy/International/gblec02a.htm; Internet; accessed April 26, 1999.

Economic Policy and Western Hemisphere Affairs, the two chief American negotiators in the U.S.-Canadian free trade talks, Peter Murphy and William Merkin, were questioned regarding the progress of the talks. After the standard references to the two thousand mile undefended border and the remarkably peaceful and cooperative relationship the United States enjoyed with Canada, Peter Murphy outlined the basic goals of the American negotiating strategy. According to Murphy, his team would seek reductions in Canadian tariff rates on items such as furniture and telecommunications equipment, and adjustments to Canadian foreign investment rules. However, Murphy also emphasized the importance of making progress on non-tariff barriers, particularly subsidies and government regulations, as well as the issue of intellectual property.[168] Murphy argued before the Committee that a fair and open trade system was incompatible with the use of subsidies by the Canadians and suggested that significant progress should be made on intellectual property issues, particularly patent rights over pharmaceuticals.[169] He also acknowledged the importance of the consultative process with both Congress and the private sector by saying

> We will be consulting with you. We will be consulting with our industries, and I

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[168]See Statement of Peter Murphy, Special Negotiator for U.S./Canada Affairs, Office of the United States Trade Representative in, U.S. Congress, House, Committee on Foreign Affairs, Subcommittees on International Economic Policy and Trade and on Western Hemisphere Affairs, *United States/Canada Trade Relations, Hearing Before the Subcommittees on International Economic Policy and Trade and on Western Hemisphere Affairs of the Committee on Foreign Affairs*, 99th Congress, 2nd session, August 12, 1986, 5; See also, USTR Clayton Yeutter, "Text of Report by United States Trade Representative Clayton Yeutter to the President on Bilateral Trade with Canada," issued September 17, 1985, in *Canadian Trade Negotiations* (Ottawa: Minister of Supply and Services, 1986), 70-72.

[169]By the mid-1980s, intellectual property rights had become a major preoccupation of the Reagan Administration's overall approach to trade. See Ronald Reagan, "Remarks at a White House Meeting with Business and Trade Leaders," September 23, 1985 in, U.S. President, *Public Papers of the United States* (Washington, D.C.: Government Printing Office, 1985), Ronald Reagan, 1985, 1127-29; *New York Times*, September 24, 1985, D26.

> can assure you you will know prior to you get[ting] it [the agreement] where we stand and what our positions are, and our objective is that through as much consultation as possible, we will be able to build a consensus for this agreement because from my own personal standpoint it is one [issue] that is important.[170]

However, Murphy, like nearly every other Administration trade official to visit Capitol Hill in the mid-1980s, was in for a rough ride from the Members of Congress. Although Murphy was testifying with respect to the Canada talks, anger with respect to the FTA was also part of the much broader Congressional dissatisfaction with trade issues discussed above.[171] But Murphy was in for a particularly harsh reception because, like those of his Administration colleagues, Murphy's statements about Congressional and private sector consultation were not convincing anyone. After a brief lecture to Murphy and Merkin about the virtues of Congressional consultation on trade matters, Congressman Robert Lagomarsino (R-California) wanted to know about the progress of the Canada talks, "not the details, but give some idea of what you have been doing."[172]

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[170]Statement of Peter Murphy, Special Negotiator for U.S./Canada Affairs, Office of the United States Trade Representative in, U.S. Congress, House, Committee on Foreign Affairs, Subcommittees on International Economic Policy and Trade and on Western Hemisphere Affairs, *United States/Canada Trade Relations, Hearing Before the Subcommittees on International Economic Policy and Trade and on Western Hemisphere Affairs of the Committee on Foreign Affairs*, 99th Congress, 2nd session, August 12, 1986, 7.

[171]By August 1986, when Murphy and Merkin were before the House Subcommittee, H.R. 4800 (the 1986 Omnibus Trade Bill) had already passed the House and was awaiting Senate consideration. See Lloyd Bentsen in U.S. Congress, Senate, Committee on Finance, *Possible New Round of Trade Negotiations, Hearing Before the Committee on Finance*, 99th Congress, 2nd session. July 23, 1986, 4. Bentsen complains that the consultative process had been so badly handled by the Reagan Administration that it nearly resulted in a disaster for the Canada talks when the Senate Finance Committee considered fast track approval for them in April 1986. The 10-10 tie vote that granted fast track authority to the talks was seen as a vote of non-confidence against the Reagan Administration on many aspects of its trade policy. See *Wall Street Journal*, April 13, 1986, 13 and April 21, 1986, 5; *New York Times*, April 22, 1986, D2.

[172]Congressman Robert Lagomarsino (R-California) in U.S. Congress, House, Committee on Foreign Affairs, Subcommittees on International Economic Policy and

Murphy dodged the question almost entirely yet had to admit that substantive issues had yet to be discussed.[173] Murphy then compounded the lack of progress by arguing for the necessity of conducting sensitive negotiations away from public scrutiny "because if you negotiate in public, in my view you aren't going to get very far anyway, because somebody is going to have a problems with it."[174] In other words, by conducting negotiations away from public view, opposition groups could be kept in the dark and prevented from effectively organizing and raising concerns. In a Congressional atmosphere that was increasingly intolerant of the vague pleadings of the Reagan Administration on trade issues, Murphy's response was especially poor. The lack of progress on substance was bad enough, but Congress had been complaining about the lack of consultation from the Administration for several years. Congressman Doug Bereuter (R-Nebraska), in particular, angrily reminded Murphy that the United States was not running a parliamentary democracy in which decisions are more readily made away from public scrutiny. Representative Bereuter continued saying

> You come to us first, not afterwards. I think the Canadians are taking advantage of us to a great extent, and have for a substantial period of time, and I think there is a distinct lack of energy and urgency with this administration and the previous in dealing with that problem.
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> Canadians have sent us an intellectual and idiosyncratic ambassador and his wife to entertain us. They employ some of the best and most expensive attorneys in the

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Trade and on Western Hemisphere Affairs, *United States/Canada Trade Relations, Hearing Before the Subcommittees on International Economic Policy and Trade and on Western Hemisphere Affairs of the Committee on Foreign Affairs*, 99th Congress, 2nd session, August 12, 1986, 21.

[173]While informal U.S.-Canadian trade discussions can be traced all the way back to the Shamrock Summit between President Reagan and Prime Minister Mulroney in March 1985, the first formal FTA talks took place on May 21-22, 1986. See Hart, *Decision at Midnight*, 155. Murphy's August testimony and admission that substantive issues had not been addressed is even more poignant given that months of informal and formal talks yielded little progress.

[174]Peter Murphy in ibid., 22.

> United States. They employ very expensive P.R. firms. We have multinational firms that are sandbagging the American people. We have a distinct lack of toughness in this administration.
>
> We don't need a free trade zone agreement with the Canadians. We have to reverse that kind of negotiating stance with the Canadians. If we are tough enough, they need to have an agreement with us, and if we go ahead with our primary focus on signing an agreement with the Canadians, the American people are more likely to come out worse as a result of that agreement than they are having an improved condition. They need an agreement with us, but there is no credibility to that kind of position unless the United States is willing to take tough action against the Canadians in a wide variety of areas.
>
> I don't see this happening. I don't see any sense of urgency anyplace about this problem, and I certainly don't see the kind of preliminary and essential, constitutionally essential, negotiation with the Congress about this matter. . . . I like the Canadians, but they are taking advantage of us, and have for years.[175]

Criticism of Murphy and the Canada talks, however was not limited to the American Congress, nor was it always wrapped up in larger trade issues. According to some of the Canadians with whom Murphy negotiated, Murphy himself was an inexperienced, junior trade negotiator who was "out of his depth" in tackling the Canada talks.[176] However, that the inexperienced Peter Murphy was assigned to the Canada talks was a symbol of the importance the Reagan Administration attached to the talks, but more importantly of the nature of the principal-agent relationship in American trade policy. According to Gordon Ritchie, a member of Canada's negotiating team, Murphy and his team would regularly arrive at meetings unprepared and ill-equipped to talk about substantive issues.[177] This assertion is supported by Alfred Eckes who, while chair of the U.S. International Trade Commission during the 1980s, observed that

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[175]Doug Bereuter (R-Nebraska) in ibid., 23-4.

[176]Gordon Ritchie, *Wrestling with the Elephant* (Toronto: Macfarlane Walter & Ross, 1997), 80; .Michael Hart, *Decision at Midnight*, 190-93.

[177]Ibid.,77.

> Other countries have more respect for history. Our principal economic competitors carefully review the records of prior negotiations and have a cadre of experienced negotiators with several generations of institutional memory. As a result, they frequently seem to exploit that advantage successfully in trade negotiations. During the bilateral free trade negotiations with Canada in 1986 and 1987, for instance, Canada fielded a team of veteran negotiators, led by Simon Reisman, who had negotiated the 1964 automobile pact. Not only did they have more experience than the Americans, but also the Canadians had a long institutional memory. They knew how specific commodity problems addressed in the free trade talks had been resolved in previous negotiations, particularly the unsuccessful attempt to negotiate similar agreement in 1947-48. The American negotiators lacked specific knowledge of this agreement or the one proposed in 1911. Oblivious to historical precedents, bright young U.S. officials rely on energy and intelligence in negotiations. Not surprisingly, they sometimes end up reinventing the wheel.[178]

However, only part of the problem was due to the poor institutional memory and inexperience of the American negotiating team. One of the central frustrations on both sides was that the American negotiating team had been shoveled off into a corner and largely forgotten by the Reagan Administration. While some of this could easily be attributed to the relative importance of the negotiations for each country, it quickly became apparent to the Canadian negotiators that Murphy and his team simply did not have the attention of high ranking officials within the Administration. As a result, a substantive exchange if ideas and positions between Murphy and the Administration with respect Canadian proposals seldom took place.[179] Compounding the uncertainty regarding the Administration's position on various issues was the resulting lack of substantive negotiating authority Murphy needed to make concessions and counter-proposals. As a result, Michael Hart, also part of the Canadian delegation to the talks, has suggested that Murphy's negotiating strategy

> appeared to be one of playing out the string. He would see what Canada was prepared to offer and at the last possible moment take this to Congress and see

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[178]Eckes, *Opening America's Market*, xvi.

[179]See Hart, *Decision at Midnight*, 190, 193, 255, 270; Ritchie, *Wrestling*, 78.

> what they were prepared to pay in return. Meanwhile, he would make as few promises as possible. In this approach, he had the natural support of his team members. . . . Thus the U.S. strategy appeared to be forged not of design or vision but of default and absence of leadership.[180]

Further adding to the problems besetting the American team, Peter Murphy's only real contacts on Capitol Hill were low level Congressional staffers. In negotiations, the American team would regularly suggest that certain proposals would not be acceptable to Congress, but without the access to Members of Congress that permitted one-on-one discussion, their assessments of what would be acceptable to Congress were guess work at best.[181] Reflecting on the talks, Michael Hart, observed that the talks never generated the political momentum necessary to force them to the top of the U.S. trade agenda in Washington:

> The U.S. team never coalesced into a team with an acknowledged leader, a sense of purpose and direction, and a clear mandate. Rather than taking direction from the US cabinet, every member looked to the interests of his or her agency and each individually kept a wary eye out for what Congress might or might not find acceptable. No one appeared to be in charge of a congressional strategy. Given the enormous importance that Congress plays in US decision-making and the constant illusions as to what would or would not fly in Congress, it was particularly galling to learn as late as July [1987] that senators and representatives and their staffers had only the faintest notion of what was being considered in the bilateral talks.[182]

The lack of knowledge on Capitol Hill about the status of the Canada talks was underscored in early 1987 in testimony before the Senate Finance Committee. In January, former USTR Robert Strauss said that he supported the Canadian negotiations but admitted that "the problem we have there is that those negotiations are the biggest political item in Canada and here nobody knows anything about them. They are unknown

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[180]Hart, *Decision at Midnight*, 190.

[181]Ibid., 270; Ritchie, *Wrestling*, 78.

[182]Hart, *Decision at Midnight*, 312-13.

here. They are on the back burner."[183] However, the testimony most indicative of the breakdown in communication between the principal and its agent on trade issues, as well as the importance attached to the Canadian talks by the USTR's office, came in February 1987 before the Senate Finance Committee. Current USTR Clayton Yeutter was asked by Senator Bill Bradley (D-New Jersey), "How many people do you have working on the Canadian negotiations directly?" To which Yeutter replied

> I can't tell you how many we have specifically assigned to the Canadian negotiations, Senator Bradley, but the answer is enough. We will do our part in that negotiation. There are a lot more working full time in Canada, and I am prepared to accept the responsibility for having fewer on this side than on that side. We believe that it is not simply a matter of numbers.[184]

Yeutter later provided the Committee with a numerical break down of the American team, but the message was clear: if the USTR was not certain of who was working on the Canadian talks, neither was the rest of the Administration.

Some ambivalence on the part of the Reagan Administration toward the Canada talks was understandable. In fact, ambivalence has been used recently by scholars as a characterization of the entire history of U.S.-Canada relations.[185] Under normal circumstances, international trade often competes in a losing battle with other domestic and foreign policy issues. Late 1986 was full of examples of issues that stole attention away from trade. Mid-term elections in early November returned control of the Senate, and its majorities on all important committees, to the Democrats, effectively wresting

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[183]Former USTR Robert Strauss in, U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st session, January 13, 1987, 44.

[184]See Senator Bradley and USTR Clayton Yeutter testimony in, U.S. Congress, Senate, Committee on Finance, *Mastering the World Economy, Hearings Before the Committee on Finance*, 100th Congress, 1st session, February 19, 1987, 112-14.

[185]See John Herd Thompson and Stephen J. Randall, *Canada and the United States: Ambivalent Allies* (Athens: University of Georgia Press, 1994).

significant control of the legislative agenda away from Republicans. Also in early November, the Iran-Contra scandal exploded onto the front pages and began occupying more and more of Washington's attention, especially that of the Administration.[186] When trade issues did capture public attention, they were most often centered around bilateral relations with Japan. However, even with these distractions, Congress could not have been impressed with the responses of the Administration to its questions regarding the Canada talks. Given the general disposition of the principal toward the agent's conduct in economic affairs in the mid-1980s, it is remarkable that talks concerning the largest two way trade in the world went unnoticed for so long. In March 1986, Alfred Eckes, then chair of the International Trade Commission, testified before Congress that in 1981 the United States enjoyed a merchandise trade surplus of $7.6 billion with Canada. However, by 1985 that figure had deteriorated into a trade deficit of $24 billion, or nearly 20% of the overall U.S. total.[187] Although the Omnibus Trade Act of 1988 sought to adjust the principal-agent relationship on overall trade policy, specific measures such as the infamous "Gephardt Amendment" of the 1986 and 1987 Omnibus bills (later dropped from the bills) that threatened to impose punitive sanctions against countries maintaining large trade surpluses with the United States, largely ignored Canada.

The poor state of the principal-agent relationship in trade policy was very much reflected in the outcome of the U.S.-Canada negotiations. On September 23, 1987, Canadian negotiators walked out of talks in Washington, citing an unwillingness on the part of the United States to address fundamental differences, and vowed not to return. The

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[186]See *Congressional Quarterly Almanac*, 1986 ed., 355-58.

[187]See Testimony of the Honorable Alfred Eckes, Commissioner, U.S. International Trade Commission, in U.S. Congress, Joint Economic Committee, Subcommittee on Monetary and Fiscal Policy, *United States-Canadian Trade, Hearing Before the Subcommittee on Monetary and Fiscal Policy of the Joint Economic Committee*, 99th Congress, 2nd session, March 12, 1986, 8-10. Japan's trade surplus with the United States was in fact much larger, peaking at over $157 billion in 1987. However, measured on a per capita basis, Canada had the largest trade surplus with the United States. See also Destler, *American Trade Politics*, 270-75.

Reagan Administration's existing fast track authority required notification of Congress of intent to enter an agreement no later than midnight October 3. Then, in a series of events that can only be described as bizarre, including the assumption of control of the American team by Treasury Secretary James Baker, the two sides managed to hammer out an agreement in two days of non-stop negotiations on October 2nd and 3rd.[188] Negotiations were concluded so quickly, that for several days afterward details were simply unavailable. When official details did emerge, they were hastily drafted and vague.[189] However, it quickly became apparent that while the agreement was sweeping and comprehensive in areas such as tariff reductions, many of the key negotiating points outlined by Peter Murphy more than a year earlier as important American interests had been dropped from the agreement.

It is not the purpose of this study to evaluate in detail stated negotiating positions relative to outcomes, but rather to suggest that a lack of oversight in the principal-agent relationship contributed to a sub-optimal final agreement for the United States. Two issues, intellectual property and subsidies, illustrate this point. As noted earlier, intellectual property was a major issue in the Administration's overall trade policy.[190] It was also a major issue for debate in Congress.[191] Representatives from California took particular

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[188]The best single account of the whirlwind talks of October 2-3, 1987 is Michael Hart, *Decision at Midnight*, especially chapter 15. See also Ritchie, *Wrestling*, 90-92, and chapter 5.

[189]See Canada, Department of External Affairs, "Elements of a Canada-U.S. Free Trade Agreement, Synopsis," October 7, 1987, in *Trade: Securing Canada's Future* (Ottawa: Department of External Affairs, 1987); *New York Times*, October 2, 1987, D1 and October 4, 1987, A1; *Wall Street Journal*, October 5, 1987, 3; Hart, *Decision at Midnight*, 336-40.

[190]See above notes 155 and 156; see also Presidential White Paper on Trade Policy, issued September 23, 1985.

[191]See for example U.S. Congress, House, Committee on Foreign Affairs, Subcommittee on International Economic Policy and Trade, *Status of Intellectual Property Protection, Hearing Before the Subcommittee on International Economic Policy and Trade of the Committee on Foreign Affairs*, 99th Congress, 2nd session, July 31, 1986;

interest in seeking additional intellectual property protections in the Canada talks. That state's broadcasting and movie production rights were of particular concern to California because of Canada's more highly regulated broadcasting industry. In House Subcommittee hearings on intellectual property in 1986, Senator Mel Levine (D-California) broke concern with Canada into three areas: "unauthorized retransmission of U.S. cable T.V. programing; the question of cultural sovereignty as the Canadians have defined it; and finally, Canada's efforts to exempt the so-called cultural industries from their campaign to establish a more liberal investment policy." Harvey Bale, Assistant U.S. Trade Representative for Trade Policy Analysis responded, saying

> We have told the Canadians that we do not view some of the proposals and the issues that
> they are addressing as legitimate cultural issues, but rather business issues. It is one thing to protect one's culture; it is another thing to protect one's industry; and a lot of what is called "cultural sovereignty," we think smaks [sic] of protectionism.[192]

Jack Valenti, President of the Motion Picture Association of America, and frequent critic of Canadian media policies weighed in with his own complaints saying

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U.S. Congress, Joint Economic Committee, Subcommittee on Trade and Productivity, and Economic Growth, *International Piracy Involving Intellectual Property, Hearing Before the Subcommittee on Trade and Productivity, and Economic Growth of the Joint Economic Committee*, 99th Congress, 2nd session, March 31, 1986; U.S. Congress, House, Committee on the Judiciary, Subcommittee on Courts, Civil Liberties, and the Administration of Justice, *Intellectual Property and Trade– 1987, Oversight Hearings Before the Subcommittee on Courts, Civil Liberties, and the Administration of Justice, of the Committee on the Judiciary*, 100th Congress, 1st session, March 18 & 26, 1987.

[192]Testimony of Harvey E. Bale, Jr., Assistant U.S. Trade Representative for Trade Policy and Analysis, Office of the USTR in, U.S. Congress, House, Committee on Foreign Affairs, Subcommittee on International Economic Policy and Trade, *Status of Intellectual Property Protection, Hearing Before the Subcommittee on International Economic Policy and Trade of the Committee on Foreign Affairs*, 99th Congress, 2nd session, July 31, 1986, 57.

> Canada, our large, and loving neighbor to the north, has adopted an investment policy which absolutely, visibly and demonstrably subtracts from our ability to move easily into the Canadian market, even as Canadian businessmen have unlimited freedom in ours. Indeed, a government-sponsored task force report is recommending that Canada inflict on the United States the roughest kind of restrictions ever, more draconian than any we face anywhere in the world. If these recommendations are activated by the Canadian Government, United States film companies will no longer be able to operate in Canada. That's as simple as I know how to put it. Nowhere on the globe are we challenged by such onerous restrictions. Nowhere. Again, Canada has slack copyright law. It is so laggard that Canadian cable systems can pick up United States television stations exhibiting American programs, bring them into their head ends, sell those programs to Canadian subscribers, and what do they pay American producers for those programs? Zero. Not one penny.[193]

On pharmaceutical patent protection in Canada, Harvey Bale from the USTR's office admitted that although his office had discussions with the Canadians on improving patent protections,

> the Canadians have not lived up to their promises to rapidly implement the law which affects this issue and the other areas that you have discussed. They have not followed through and done what is right. But it is going to be a subject, I think, of continuing high-level consultations, both in the context of the Free Trade Agreement— And outside of the Free Trade Agreement.[194]

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[193]Testimony of Jack Valenti, President, Motion Picture Association of America, Inc., in U.S. Congress, Joint Economic Committee, Subcommittee on Trade and Productivity, and Economic Growth, *International Piracy Involving Intellectual Property, Hearing Before the Subcommittee on Trade and Productivity, and Economic Growth of the Joint Economic Committee*, 99th Congress, 2nd session, March 31, 1986, 27. These sentiments regarding Canada were largely echoed in the Testimony of Frank G. Wells, President, Walt Disney Co., in ibid., 77. Disney's main complaint was with respect to Canadian investment policy. The FTA's investment provisions left intact Canada's ability to protect its "culture." See Canada, External Affairs, "Elements of a Canada-U.S. Free Trade Agreement,"3-5; *Congressional Quarterly Almanac*, 1987 ed., 663.

[194]Testimony of Harvey E. Bale, Jr., Assistant U.S. Trade Representative for Trade Policy and Analysis, Office of the USTR, in U.S. Congress, House, Committee on Foreign Affairs, *Status of Intellectual Property Protection, Hearing Before the Subcommittee on International Economic Policy and Trade of the Committee on Foreign Affairs*, 99th

Jack Valenti cautioned legislators in 1986 that "if you don't do this [deal with intellectual property], I promise you, we'll be back here next year and could replicate this hearing."[195] In fact, in 1991, Valenti was again before Congress and fulfilled his own promise by largely repeating his 1986 testimony.[196] The reason for his displeasure in 1991 was that when the details of the U.S.-Canada Free Trade Agreement emerged, intellectual property had been left out entirely and Canada had retained its "full capacity to support cultural industries in Canada."[197] As for pharmaceutical patents, according to Michael Hart, Canada might have been willing to include a substantive chapter on intellectual property, including stronger drug patent protection, in the agreement in exchange for an exemption from Section 337 of the 1930 Tariff Act (Smoot-Hawley). Section 337 permitted U.S. companies with expedited procedures for protection from imports alleged to be tainted by

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Congress, 2nd session, July 31, 1986, 57.

[195]Testimony of Jack Valenti, in U.S. Congress, Joint Economic Committee, Subcommittee on Trade and Productivity, and Economic Growth, *International Piracy Involving Intellectual Property, Hearing Before the Subcommittee on Trade and Productivity, and Economic Growth of the Joint Economic Committee*, 99th Congress, 2nd session, March 31, 1986, 53.

[196]"As you well know, Mr. Chairman, there is unhappily engraved on the forehead of the United States- Canada Free Trade Agreement a thing called a cultural exclusion, which means movies, television, sound recordings, books, are exiled– thrown over the side, won't even be discussed, in that compact between those two countries." See U.S. Congress, Senate, Committee on Finance, *Review of the Uruguay Round: Commitments to Open Foreign Markets, Hearings Before the Committee on Finance*, 102nd Congress, 1st session, April 17-18, 1991, 62.

[197]See Canada, External Affairs,"Elements of a Canada-U.S. Free Trade Agreement," 3; *Congressional Quarterly Almanac*, 1987 ed., 663. CQ reported that the FTA "*urged* more compatible laws protecting patents and other intellectual property rights [emphasis mine]." In 1996, Canada was placed on a "watch list" under the "Special 301" provisions for restrictions it placed on providers of Direct-to-Home satellite T.V. systems. See Office of the United States Trade Representative, *USTR 1996 Fact Sheets on Special 301 on Intellectual Property* at http://www.ustr.gov/reports/301report/factsheets.html; Internet; accessed April 26, 1999.

intellectual property infringements.[198] The United States claimed that generic drug manufacturers in Canada were unfairly benefitting from American research and development costs without due compensation for patent rights. The Americans had been pressuring the Canadian Government for several years to make changes to its patent laws.[199] When these issues arose during the Free Trade negotiations, the United States was unwilling to exempt Canada from Section 337 and Canada, therefore, was willing to go no further on pharmaceuticals than the provisions of Bill C-22 then working its way slowly through Parliament.[200] As a result, intellectual property, one of the primary components of the Reagan Administration's overall trade policy, was dropped from the trade

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[198]Hart, *Decision at Midnight*, 306.

[199]One important point of contention centered around Canada's compulsory licensing practices in which firms could apply to the Commissioner of Patents for a compulsory license to use an already patented process to manufacture generic versions of drugs in Canada. Compulsory licencing was intended to introduce lower-cost competition to the Canadian pharmaceutical market. A Royal Commission into the pharmaceutical industry in 1985 concluded that changes to compulsory licensing should be made to allow patent-holding firms more of the benefits of research and development. In particular, the Commission recommended that a four year period of exclusivity to patent holder be imposed and created a formula for royalty payments to be made by firms that hold present and future compulsory licences. See *Summary Report of the Commission of Inquiry on the Pharmaceutical Industry* (Ottawa: Minister of Supply and Services, 1985); Y. Kotowitz, *Issues in Patent Policy with Respect to the Pharmaceutical Industry* (Ottawa: Minister of Supply and Services Canada, 1986), 1-17. See also Joel Lexchin, *Pharmaceuticals, Patents and Politics: Canada and Bill C-22* (Ottawa: The Canadian Center for Policy Alternatives, 1992), 3-5. He argues that the provisions of Bill C-22 ending compulsory licensing were a concession extended to the United States in exchange for a free trade agreement.

[200]Ibid., 341, 354. Ironically, changes made to Section 337 of the Tariff Act of 1930 by the Omnibus legislation in 1988 were ruled by a GATT panel in 1989 to be inconsistent with GATT rules because they contained "too many distinctions between domestic and foreign patent infringers." See note 95 and U.S. Congress, House, Committee on the Judiciary, Subcommittee on Courts, Intellectual Property and the Administration of Justice, *Intellectual Property, Domestic Productivity and Trade, Hearing Before the Subcommittee on Courts, Intellectual Property, and the Administration of Justice, of the Committee on the Judiciary*, 101st Congress, 1st session, July 25, 1989, 66-70,103-106, 180.

agreement.[201]

Much the same story can be told for subsidies. In the final agreement, both sides agreed to maintain their respective national laws and procedures on subsidies and dumping and to refer future disputes to the newly created binational dispute resolution panel, the creation of which was itself a major American concession.[202] The elimination of most tariffs between the two countries has more fully exposed some of the more difficult trade irritants between the two countries. In the decade since the Free Trade Agreement, all of these issues have, at one point or another, threatened to push Canada and the United States into a bitter trade battle. In a long-running bilateral dispute, Canadian "stumpage" fees paid by forestry companies to the provincial and federal governments to cut trees on public land have been seen by the United States as artificially low. Such cost advantages have been viewed as government subsidies that unfairly enhance the competitiveness of Canadian wood products in the United States.[203] In late 1998, American farmers staged a temporary border blockade trucks carrying Canadian agricultural commodities bound for U.S. markets because of "unfair" government subsidies to Canadian farmers, and although promises by both sides ended the dispute temporarily, the basic irritants remain.[204] Lastly, the Canadian "cultural" exemption from most provisions of the FTA has threatened to lead to a bilateral trade war over so-called split-run magazine publications. The Canadian

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[201]*New York Times*, October 5, 1987, D5. See also Canada, External Affairs "Elements of a Canada-U.S. Free Trade Agreement." The External Affairs document does not even mention intellectual property as an issue for future discussion. See also, Hart, *Decision at Midnight*, 382-3, 336, 382-383.

[202]Canada, External Affairs, "Elements of a Canada-U.S. Free Trade Agreement," 7-8. The American refusal to assent to a mechanism for resolving disputes was one of the major reasons for the Canadian walk-out on September 23, 1987. See *Wall Street Journal*, September 24, 1987; See also, Canada, Department of External Affairs, *The Canada-U.S. Free Trade Agreement*, October 12, 1987, (Ottawa: Department of External Affairs, 1987), 261-66.

[203]See *Globe and Mail*, January 2, 1999, B1.

[204]*Globe and Mail*, October 3, 1998, B3.

position holds that economies of scale from publication in the United States give American publishers an unfair advantage in the Canadian market that indigenous publishers do not enjoy, thus threatening their existence. According to the current (1999) Canadian Heritage Minister, Sheila Copps, the threat to magazine publishers is also a threat to Canadian culture. The United States has objected to the ban on magazine imports with advertising directed at Canadians, the 1995 excise tax of 80% imposed on split-run magazine imports, and the favorable postal rates given to Canadian publications that amount to a government subsidy. This particular dispute has flared up in several guises, including a 1997 World Trade Organization (WTO) challenge of Canadian law that eventually vindicated the American position. More recently, the Canadian Government has proposed a new set of laws (Bill C-55) that largely replaces those struck down by the WTO. If passed, the new laws would make it illegal for Canadian companies to advertise in foreign magazines aimed primarily at Canadian readers. The United States has threatened to retaliate if C-55 is passed, and although the two sides were talking as of February 1999, C-55 still threatens to generate significant friction.[205]

International trade negotiations are not a perfect science, and the agreements eventually spawned from negotiations are obviously the product of significant compromise and haggling by all participants. In the case of the Free Trade Agreement, however, American negotiators failed to address during the talks several of their self-proclaimed priority issues that have since continued to cause significant problems. Some of these failures may be attributable to the need for compromise. However, the evidence suggests that the American approach to trade policy with Canada during this period was really the larger American trade picture in microcosm. In dealing with Canada, the United States was without solid leadership, direction, or clear policy goals. The American negotiating team and its strategy were ill-conceived by an Administration whose economic leadership

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[205]See Office of the United States Trade Representative, Press Release, *United States to Take Action if Canada Enacts Magazine Legislation*, October 30, 1998 at http://www.ustr.gov/releases/1998/10/index.html; Internet; accessed April 26, 1999. *Edmonton Journal*, September 15, 1998 A8; *Globe and Mail*, October 31, 1998, A3, and January 4, 1999, A14.

was clearly on the defensive in the late 1980s. However, most importantly, many of these factors were both the cause and result of a breakdown of the principal-agent relationship on trade issues in this period. Although the U.S.-Canada Free Trade Agreement passed with large bipartisan majorities in both Houses of Congress, Congress demonstrated its displeasure with the Administration by concentrating not on what was in the agreement, but what was left out.[206] When legislation to implement the free trade agreement became law in September, it was the last major agreement concluded by the United States under pre-Omnibus institutions.

When the 1988 Omnibus Trade and Competitiveness Act became law on August 23, 1988, it dramatically altered the conduct of the principal and agent in the trade policy process. The Canada agreement had, in effect, squeaked into existence just before important changes could be made. The first real test of the post-Omnibus principal-agent relationship came in June of 1990 when Presidents Bush and Salinas announced that the United States and Mexico would seek a free trade agreement. In stark contrast to the period of the FTA, principal and agent, for the first time in years, at the outset struck a more cooperative stance with each other that further demonstrates the centrality of agency in the American policy process.

Having said this, however, several factors admittedly set the U.S.-Mexico initiative apart from previous trade negotiations in important ways and directly contributed to an increase in interest and cooperation on the part of the principal and agent. Because Mexico was still part of the developing world, negotiations drew the attention of American labor and environmental groups who worried that the meshing of developed and developing economies would produce an exodus of jobs out of the United States as the competitive advantages of lower Mexican wage scales lured American manufacturers

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[206]See U.S. Congress, Senate, "United States-Canada Free Trade Agreement Implementation Act,"100th Congress, 2nd session, *Congressional Record*, September 19, 1988, obtained from Nexis-Lexis online information service, August 15, 1998; *Congressional Quarterly Almanac*, 1988 ed., 222-3. The implementation legislation was approved by the House on August 9, 366-40 and by the Senate September 19, 83-9.

south of the Rio Grande.[207] In addition to concern over lax environmental standards, environmental groups worried that as pressures to harmonize economic policies took hold under free trade, the agreement's dispute resolution mechanisms could be used by Mexico to challenge higher American ecological product standards by arguing they were unfair restrictions on Mexican trade.[208] When Canada joined the negotiations in February 1991, the stakes were raised as all three countries considered creating one of the largest free trade areas in the world. Unlike the FTA , which generated fierce political debate in Canada but not in the United States, NAFTA generated significant political debate in all three countries and became a major issue in the U.S. presidential election of 1992.

While all of these factors may have contributed to increased participation in the NAFTA process by a broader cross-section of society than in previous talks, only part of the reasons stems from the higher stakes involved and election year politics. The most profound, if simple, differences in the process under which NAFTA was handled came about from the changes to agency made in the late 1980s. The most striking, and perhaps most important, feature of principal-agent interaction in the post-Omnibus era was the change in tone that principal and agent took towards trade, and which was first demonstrated during the 1991 debate over fast track extension. As we have seen, that change in tone resulted in frank and frequent consultation between the Administration, particularly the Office of the USTR, and Congress that led to the extension of fast track authority for NAFTA. That consultative process was still replete with the familiar, by then somewhat ritualized, rhetorical arguments from both sides that included the

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[207]During the 1992 general election, presidential candidate Ross Perot repeatedly charged that low wages and lax environmental controls in Mexico would create a "giant sucking sound of jobs being pulled out of this country [United States]" as American firms relocated to take advantage of cost differentials. See "Presidential Debate in East Lansing, Michigan," October 19, 1992, in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: Government Printing Office, 1992), George Bush, 1992, 1859-1860.

[208]Conversely, American industry could also lobby to have domestic environmental laws relaxed by arguing that looser Mexican standards give them a comparative cost advantage that cannot be matched in the United States.

Administration raising of the specter of Smoot-Hawley and regular lectures from Congress to the Administration on the need for improved leadership and consultation on trade issues. However, such rhetoric was also tempered by the recognition by both sides that each needed the other in order to manage American trade policy. An even more impressive test of the new Omnibus institutions was the continuation of that cooperative and consultative effort long after the Administration received its sought-after fast track authority.

On September 18, 1992, just fifteen months after the extension of fast track authority, President Bush notified Congress of his intent to enter into the NAFTA with Canada and Mexico. In doing so, he called the entire process of reaching that stage a "shining example of bipartisan cooperation."[209] However, more than an effort on the part of Democrats and Republicans to bridge differences on trade, it was a shining example of how the principal and agent can interact successfully in the formation of trade policy. In his message to Congress, the President again made reference to his May 1, 1991, response to the concerns of Congress as expressed in the Rostenkowski-Bentsen letter. Both then and in September 1992, the President promised to cooperate extensively with Congress on labor and environmental issues as they related to NAFTA. Although NAFTA as a campaign issue grew in importance for the Bush Administration as the 1992 election drew near, the Administration's efforts were as much designed to capture points for partisan gain as they were in direct response to the demands of the principal that it be part of a consultative and cooperative process on trade. On the same day President Bush notified Congress of his intent to enter NAFTA, the Administration issued a report outlining in detail how it and NAFTA had fulfilled the May 1 commitments. In part, it read,

> The successful completion of the NAFTA reflects an unprecedented partnership between the President and the Congress. On March 1, 1991, President Bush

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[209]See President Bush, "Letter to Congressional Leaders on the North American Free Trade Agreement," September 18, 1992, in U.S. President, *Public Papers of the Presidents of the United States* (Washington, D.C.: Government Printing Office, 1992), George Bush, 1992, 1595.

> notified the Congress of his intent to enter into free trade negotiations with Mexico and Canada, and requested an extension of the "fast track" procedures for Congressional review and implementation of trade agreements. On May 1, 1991, in response to concerns raised by Members of Congress, the President committed to addressing concerns with respect to adjustment, labor mobility, worker rights, and environmental protection in the NAFTA agreement itself and in parallel cooperative activities. Consistent with the letter and the spirit of the fast track, the Administration further committed to a process of intensive Congressional and private sector consultations throughout the negotiations. On this basis, Congress endorsed moving forward with the NAFTA by extending the fast track procedures. As this report indicates, the Administration has fulfilled, if not exceeded, the commitments made in the President's May 1 Response to Congress.[210]

The report detailed the impressive, and unprecedented, levels of consultation and cooperation with Congress. Whereas the text of the FTA was unavailable to anyone several days after it was concluded in October 1987, even the earliest drafts of NAFTA negotiating texts were made available to all members of Congress as well as to each of the thousand plus private sector advisors to the Office of the USTR.[211] All of this prompted House Ways and Means Committee Chairman Dan Rostenkowski to publicly observe in June 1992 that the Administration had been relentless in keeping Congress informed throughout the negotiations and could not be faulted for secrecy.[212] Furthermore, by the Administration's own count, "since the NAFTA negotiations began in mid-1991, Ambassador Hills [USTR] and her interagency negotiating team have held nearly one thousand briefings and consultations with Congress, private sector advisors, trade associations, business groups, and the public at large. This amounts to an *average of three briefings per work day* since the talks were launched."[213] Furthermore, unlike the FTA

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[210]*Report of the Administration on The North American Free Trade Agreement and Actions Taken in Fulfillment of the May 1, 1991 Commitments*. Issued September 18, 1992, US GPO FEB 93-5908, 6.

[211]Ibid., 7.

[212]Quoted in ibid.

[213]Ibid., 65. Note the stark contrast between the details divulged as part of the Executive's effort on NAFTA in 1991 and 1992 with Clayton Yeutter's admission before

where private sector interests were unable to penetrate and actively participate in negotiations, in part because of their relative secrecy, the Administration actively sought out private sector input during the NAFTA process.[214] In fact, the Office of the USTR had forty advisory committees, composed of more than one thousand representatives of industry, labor, consumer and environmental interests, and on committees of state and local government officials.[215] The consultative process with the private sector in particular was so extensive that there was nearly unanimous agreement on the part of the 44 member Advisory Committee for Trade Policy and Negotiations (ACTPN) that NAFTA should be approved by Congress. With the exception of the two representatives from labor organizations, the committee believed that "the agreement substantially meets the objectives set out by the ACTPN in September 1991."[216] On intellectual property rights, a subject dropped in the FTA, the ACTPN believed "that the provisions in intellectual property as they pertain to Mexico substantially meet most of the ambitious negotiating objectives and are acceptable."[217] However, like all agreements, imperfections remained, especially on intellectual property rights. "It should be emphasized," the ACTPN report continued,

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the Senate Finance Committee in February 1987 that he had no idea how many individuals were assigned to the bilateral talks with Canada.

[214]Rules for private sector consultation in trade negotiations were enshrined in Section 135(e) of the Trade Act of 1974, but for years had been largely ignored. The 1988 Omnibus Trade and Competitiveness Act strengthened these rules.

[215]*Report of the Administration on The North American Free Trade Agreement and Actions Taken in Fulfillment of the May 1, 1991 Commitments.* Issued September 18, 1992, US GPO FEB 93-5908, 65-68.

[216]*A Report to the President, the Congress, and The United States Trade Representative Concerning the North American Free Trade Agreement. Submitted by The Advisory Committee for Trade Policy and Negotiations (ACTPN).* September 15, 1992, US GPO DEC 93-29440, III-IV.

[217]Ibid., 63.

> that the ACTPN views the decision to accede to Canada's insistence on a cultural exemption with great regret. The ACTPN urges that this exemption be addressed at the earliest possible opportunity. In the meantime, the cultural exemption should not be considered a precedent for other intellectual property negotiations, such as the GATT TRIPS negotiations.[218]

The Industry Functional and Sectoral Advisory Committee's (IFAC) report to the President and Congress concurred with respect to the intellectual property provisions of NAFTA saying that "taken as a whole, the NAFTA intellectual property provisions represent the highest standards of protection and enforcement so far achieved by U.S. negotiators."[219] However,

> Under the NAFTA, Canada would not be obligated to provide the benefits secured in the intellectual property chapter to the "cultural industries." Canada would be free to discriminate against these industries through the denial of national treatment or through the failure to provide the NAFTA minimum level of protection. The industries affected are some of America's most productive and competitive: the motion picture, TV and video production industries; the music and recording industries; the book, journal, magazine and newspaper publishing industries; and the U.S. radio, television cable, and satellite industries.[220]

Thus, Canada's so-called cultural industries, particularly magazine publishing, have continued to be a source of irritation in U.S.-Canada relations.[221]

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[218]Ibid.

[219]*Report to the President, To Congress, To the Secretary of Commerce, and to the United States Trade Representative on The North American Free Trade Agreement, The Reports of the Industry Functional and Sectoral Advisory Committees* (IFACs/ISACs) September 8, 1992, US GPO DEC 93-29442, 39.

[220]Ibid., 49-50.

[221]Another, related, source of ongoing bilateral irritation concerns Canadian copyright law. On April 25, 1997, Bill C-32 received Royal Ascent in the Canadian Parliament and was intended to modernized Canada's copyright laws. Among its provisions was a tax on blank audio and video cassette tapes to be distributed to Canadian holders of audio and visual copyrights. On April 30, 1997, the USTR placed Canada on its Special 301 "watch list" because C-32 denied proceeds of that tax to American copyright

In spite of its failure to achieve all of the goals set out by the various private and public interests, the NAFTA process was notable for the extensive role played by private sector advisory groups. The private sector had for the first time played an official, significant, substantive, open, and mandated role in the trade policy process. Pre-negotiation recommendations were made by a broad cross-section of American private sector interests on a wide variety of issues to U.S. negotiating teams, and those recommendations were, by and large, adhered to.

While no agreement is without its critics or without its flaws, the impressive shift away from secrecy and confrontation during the NAFTA process brought about by the alteration of the principal-agent relationship marked a turning point toward more cooperative and productive trade policy formulation.[222] Omnibus had altered the contractual relations between the principal and agent. NAFTA was the first substantive test of the principal's experiment in trying to provide both the carrots and sticks to its agent to maximize economic benefit. Congress had given, and in some instances forced upon, the agent important foreign policy tools in Omnibus as well as the 1991 extension of fast track. The principal clearly wanted America's liberal economic policies to continue, and so delegated its authority. However, while Congress wanted and obtained a greater voice in the foreign economic policy process, the post-Omnibus rules set out in 1988 stopped well short of a reassertion of Congressional prerogatives over trade policy. While many assessments of both the FTA and NAFTA have been positive in terms of their broad economic impact, the stark contrast exhibited in the U.S. approach to each of these agreements provides a window on how institutional change in the U.S. policy process can have a dramatic impact on both the process of obtaining and the realization of American

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holders thereby violating national treatment provisions of NAFTA. See Office of the United States Trade Representative, *1998 National Trade Estimate* at http://www.ustr.gov/reports/nte/1998/contents.html; Internet; accessed April 26, 1999.

[222]NAFTA's critics in both the U.S. and Canada continue to charge that the side agreement on labor is relatively weak and has provided little substantive recourse to Mexican labor groups seeking improvements in working conditions and wages. See *Globe and Mail*, August 29, 1998, A11.

trade policy objectives.[223]

[223]See Executive Office of the President, *Study of the Operation and Effect of the North American Free Trade Agreement* (Washington, D.C.: Government Printing Office, 1996), reporting indicates that while the economic gains due to increased trade were modest in the first three years of NAFTA, trade ties did help lessen the deleterious impact of the 1994 devaluation of the Mexican peso. The report's assessment of the operation of the environmental and labor side agreements was also positive. See also, Joshua Avram, "Free Trade at 10," *Alberta Report* 24 (October, 1997): 6-9.

CHAPTER 8

PARTISAN POLITICS

Critics of agency as a foreign economic policy lens might disagree with its tendency to treat Congress as a unified decision making body in which partisan politics have negligible impact. Judged by the displeasure displayed by members of Congress in the late 1980s and early 1990s, it is worth considering whether political partisanship is a significant factor in the policy-making process. Because agency almost assumes that the principal speaks with one voice, as perhaps it would were Congress a corporation instructing its sales representatives, partisan disagreements in Congress do complicate an agency framework. However, partisan conflict over trade has also been demonstrated to be more complicated than the simple dichotomies of free trade versus protectionism or Democrats versus Republicans often depicted in economic policy literature. As a result, while a consideration of partisan politics complicates agency to some degree, it does not ultimately undermine agency's utility as an economic policy lens.

As a political issue, the tariff has been one of the most important and contentious in American history. Robert Pastor, for example, has suggested that until the end of the Kennedy Round of GATT negotiations, foreign economic policy was tariff policy. Through much of the nineteenth century, tariff revenues contributed as much as ninety percent of all government revenue.[224] While in the late twentieth century free trade and open markets have been linked to economic prosperity, in the last century, the opposite was true.[225] Partisan positions on the tariff have their roots in some of the ante-bellum

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[224]Pastor, *Congress and the Politics*, 69-75.

[225]Eckes, *Opening America's Market*, 28.

political and economic conflicts that eventually led to the Civil War. From its earliest roots as part of the anti-Nebraska coalition in the 1850s through to the Great Depression, the Republican party consistently advocated the necessity of high tariffs to protect American industry. In the industrial centers of the North, high tariffs shut out foreign goods and fostered, if artificially, infant American industry. The agrarian South, in contrast, tended to favor lower tariff rates to reduce the purchase price on manufactured goods. Southern support for the Democratic party through the mid-nineteenth century was based partly on free trade platforms. However, while Democrats from 1860 through to the Great Depression reveled in exposing the corrupt relationship between inefficient industries and Republican politicians, Democrats vacillated between open avowal of free trade and protective policies.[226]

William Keech and Kyoungsan Pak have argued that until approximately the 1960s, party positions, particularly Republican positions, on the tariff remained relatively static. On the Presidential level, however, led to some extent by the changes initiated by the Reciprocal Trade Agreements Act of 1934, party positions began to converge as both parties moved away from any presumptions of protectionism and toward a free trade orientation. Both sides increasingly trumpeted the virtues of free but "fair" trade and open markets for American goods.[227] Although small differences in Presidential platforms continue to exist, they have rarely been part of partisan confrontation based upon clearly drawn alternative ideologies on trade issues.[228] However, on the Congressional level, party

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[226]Ibid., 28-36. Dryden, *Trade Warriors*, 11.

[227]Zeiler, *American Trade and Power*, chapter 1, outlines the origins of "fair-trade" doctrine that Zeiler argues originated out of the growing need in the 1960s to balance the protectionist needs of domestic producers with larger foreign policy goals, such as providing open U.S. markets for Western European exports and solidifying the Western alliance during the Cold War.

[228]William R. Keech and Kyoungsan Pak, "Partisanship, Institutions, and Change in American Trade Politics," *Journal of Politics* 57 (November 1995): 1135; See also Anthony Downs, *An Economic Theory of Democracy*, Chapters 2, 4 & 8. These assertions are supported by Downs who has demonstrated that self interested legislators seek, through their party apparatuses, to maximize their re-election chances through party

positions on trade have been more complicated. Keech and Pak argue that Republicans and Democrats essentially switched their traditional positions during the 1960s, as Democrats began emphasizing the effects of import competition and became more frequently associated with organized labor groups.[229] While party positions on trade have periodically changed, trade issues as issues in the electoral fortunes of legislators have also changed, particularly in the postwar era. Wendy Hansen and Thomas Prusa have argued that median legislative voter models can explain shifts in U.S. tariff policy prior to 1934. In other words, as the trade policy preferences of the average voter in Congress have shifted, so too has U.S. tariff policy, indicating that partisan positions on the tariff played an important role in electoral outcomes. However, after 1934, such models fail to explain shifts in U.S. policies suggesting that electoral gains from partisan positions on trade were more uncertain.[230]

I. M. Destler argues that although Congress and the Executive seem to be struggling over policy outcomes, there is asymmetry in the stakes. For individual members of Congress, direct control over trade policy is not a necessary means to their broader goal of enhancing their immediate re-election concerns or their political standing among Washington's power brokers.[231] Trade presents legislators with a particularly nasty conundrum. Most of the benefits of freer trade in a continental economy are broadly spread in terms of slightly lower costs for consumers and producers in a broad spectrum of industries. However, adjustment costs from free trade in terms of relocation or closure

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platforms that will garner the most votes. In a two party system, party platforms converge on issues that an overwhelming majority of voters agree upon. Platforms tend to be full of vague positions so as not to alienate potential voters will extreme positions and are seldom linked to any ideological position.

[229]Keech and Pak, "Partisanship, Institutions, 1131-33.

[230]Wendy L. Hansen and Thomas J. Prusa, "The Role of the Median Legislator in U.S. Trade Policy: A Historical Analysis," *Economic Inquiry* 35 (January 1997): 97-107.

[231]Destler, "U.S. Trade Policy-Making in the Eighties," 255.

of inefficient factories tend to be highly focused in specific districts.[232] Destler further argues that the majority of legislators for whom trade is only an occasional concern, simply advocate the cause of those specifically affected in their own districts while continuing to ally themselves with their broader political power base.[233] Stanley Nollen's and Dennis Quinn's examination of roll call voting patterns in the 100th Congress (1987-88) on trade issues supports Destler's argument. They concluded that while partisan politics was a contributing factor to voting patterns, in no way was it the only factor influencing Congressional votes. Nollen and Quinn first argue that because debate over trade is no longer just about free trade or protectionism, but also includes "fair trade" and "strategic trade" as legitimate policy positions, the choices of legislators and their reasons for them have become much more varied.[234] Nollen and Quinn concluded that a variety of factors, including political action committee contributions, the nature of economic activity in a legislators home district, and unemployment rates in those districts all had significant impacts upon voting patterns in 1987-88.[235]

Finally, Susanne Lohmann and Sharyn O'Halloran have examined the role of partisan conflict in legislative battles between Congress and the Executive over trade policy. Their evidence suggests that trade bills passed during times of high partisan conflict between Congress and the Executive (when different parties control the Legislative and Executive branches) have nearly always resulted in constraints being placed upon the President's discretion over trade. On the other hand, under unified government, when one party controls both Congress and the White House, Presidential

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[232]See Susanne Lohmann and Sharyn O'Halloran, "Divided Government and U.S. Trade Policy: Theory and Evidence," *International Organization* 48 (Autumn 1994): 601.

[233]Destler, "U.S. Trade Policy-Making in the Eighties," 255.

[234]Stanley D. Nollen and Dennis P. Quinn, "Free Trade, Fair Trade, Strategic Trade, and Protectionism in the U.S. Congress, 1987-88," *International Organization* 48 (Summer 1994): 491-525, especially 505-506.

[235]Ibid., 517-522.

authority has nearly always grown.[236] As a result, argue Lohmann and O'Halloran, levels of U.S. protectionism in the postwar period can be directly linked to partisan conflict between Congress and the Executive.[237] However, while these findings seem to contradict assertions that partisan politics are not a significant issue on trade matters, Lohmann and O'Halloran, like Destler, also assert that one of the main goals of Congress as a whole in delegating its authority to the Executive at all is to end up with a trade policy compromise that Congress would never have enacted on its own. "Under divided government," they argue,

> the President's use of delegated authority may be constrained, but depending upon economic conditions, the constraints imposed may not be binding. Moreover, if Congress chooses to delegate partially its policymaking authority, procedural constraints do not lead to the full unraveling of the President's discretionary powers. . . . When the constraints imposed on the President's powers are binding, the President must partially accommodate the *ex post* demands of Congress. The resulting outcome will then be closer to the one that would be obtained if Congress were to pass trade legislation itself.[238]

In other words, despite the partisan wrangling that exists, trade legislation, even under divided government, still nets policies that Congress itself would not or could not have passed on its own. Partisan politics then is a mixed bag as far as its impact on American trade policies in concerned. In the period under investigation here, a Democratically controlled Congress in 1988 appeared ready to impose severe restrictions on the Republican Executive's trade policy discretion. However, as we have seen, when the Omnibus bill was finally enacted, many of the most draconian proposals made during the debate were left out of the final legislation. Rather than crippling the agent's ability to conduct trade negotiations, Congressional restraint upon the Executive tilted trade policies towards priorities set by Congress but did not result in trade outcomes that could have

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[236]Lohmann and O'Halloran, "Divided Government," 618.

[237]Ibid., 626.

[238]Ibid., 629; Destler, "U.S. Trade Policy-making in the Eighties," 255-256.

been created by Congress alone. In essence, partisan conflict affects trade policy outcomes, but in a way that can be accommodated within the principal-agent framework developed in this paper. Both principal-agent theory and practical necessity suggest that Congress needs an agent in the formation of foreign economic policy and to help manage increasingly interdependent economic relations. Where partisan politics models fall short is in providing a systematic rationale for Congressional behavior other than one based upon *ad hoc* contingencies of the period or for why the policy process regularly nets middle ground outcomes in spite of ostensibly bitter partisan bickering. Agency does not rely upon such *ad hoc* explanations and instead provides a rationale for the reciprocal nature of the principal-agent relationship and why the principal in particular does not, and has not for most of the postwar period, fired its agent and reasserted its Constitutional prerogatives over foreign commerce. Furthermore, party politics on trade issues seems particularly tenuous as an explanation for trade outcomes given the disparate local economic interests represented in Congress. How do widely disaggregated economic interests translate themselves directly into broad bases partisan political positions on trade issues when so many different sectoral interests and positions on policy are possible? As a result, the arguments of Destler as well as Nollen and Quinn lead to the much more plausible position that partisanship on trade issues is much more varied and difficult to generalize about than some scholars acknowledge.

CHAPTER 9

CONCLUSION

One of the risks inherent in taking a theoretical approach to the social sciences and humanities lies in its longevity as a descriptive, explanatory, and predictive powers after being repeatedly tested under different circumstances. On the one hand, theories have utility insofar as they enable researchers to form new hypotheses when applied to new sets of circumstances. On the other hand, risk lies in utilizing theories that are so broad as to be unfalsifiable under any circumstances and are thereby of little use in generating new hypotheses. Unlike the physical sciences, where the scientific method and controlled laboratory conditions enable researchers to replicate experiments to test hypotheses again and again, examining the human condition rarely lends itself to similar lab-like conditions.

This study, like others in the social sciences and humanities, has its own inherent strengths and weaknesses, brought about, in part, because of its reliance upon economic theory as a framework for examination. We have seen how agency as an American foreign economic policy lens seems to describe, explain, and predict the actions of Congress and the Executive during the 1980s and early 1990s, but this approach also has several shortcomings that must be acknowledged and merit further study. First, agency should perhaps be more appropriately considered a foreign *trade* policy lens, rather than a broad approach for describing all of American foreign economic policy. While trade is one of the most important parts of American economic policy, foreign investment and assistance policies are also important aspects of the overall foreign economic policy equation, and agency may not adequately explain and predict them. Monetary policy, also, is part of overall American foreign economic policy because of its important impact abroad. As is the case with trade policy, agency plays an important role in the formation of American

monetary policies in that the Federal Reserve has been delegated a significant amount of authority by Congress to determine policies. The Fed's quasi-independent nature and relative freedom from dramatic institutional change seem to set it apart from other situations, such as trade policy, in which agency between Congress and the Executive branches exists. However, agency with respect to Fed activities has one characteristic that sets it apart from that observable in trade policy, the relative symmetry of interests on the part of both principal and agent. Whereas the agency relationship between Congress and the Executive on trade issues is a partial delegation of authority to an agent with different interests and full of the constraints that make monitoring so important, the Fed enjoys a near complete delegation of authority, primarily because of the relative similarity in policy goals on the part of both principal and agent. That the Fed's basic function and its relationship as agent to the principal has seldom changed is additional evidence that agency, while clearly in operation, may not be the most descriptive or explanatory means of viewing the Fed or explaining institutional change in the Fed's operation.

If agency is not quite appropriate as a broad lens for examining all of American foreign economic policy, it is still more inadequate as a general foreign policy lens. For example, agency does a poor job of explaining American involvement in Vietnam, President Nixon's trip to China in 1972, the Iran-Contra Affair in the mid-1980s, or the decision to send U.S. troops to the Persian Gulf in 1990. If other areas of foreign economic policy lack a the formal delegation of authority present in trade matters, broader foreign policy considerations lack even more. Unlike the authority over foreign commerce which rests explicitly with Congress, other foreign policy powers are distributed by the Constitution between both the Executive and Legislative branches. For example, Congress holds appropriations powers and the ultimate power to declare war, yet the President is vested with the power to conduct foreign policy via the treaty power and the President's role as Commander in Chief of the military.[239] In the many Congressional committees that deal with military affairs, national security, and other broad areas of foreign policy, there is

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[239]See *U.S. Constitution*, article 1, section 8-9; article 1, section 2.

cooperation between the Administration and Congress, as well as significant lobbying of Congress by the Administration to garner support for new policies. However, aside from standard oversight hearings by Congress, no formal delegation of responsibility has taken place in other areas of foreign policy as has been the case with foreign commerce since 1934.

Before claiming that agency is an infallible lens through which to describe, explain, and predict American trade policy, it must also be tested in other periods of American history. In brief, while agency seems particularly applicable to the period under examination here, it does not so readily lend itself to explaining American policies in all other periods. For example, prior to the 1934 Reciprocal Trade Agreements Act, there were few examples of a substantive agency relationship between Congress and the Executive on trade issues. As outlined in article 1, section 8 of the Constitution, Congress, before 1934, retained exclusive control over the regulation of foreign commerce, primarily through setting tariff rates. Agency could be employed in the pre-1934 period as an argument for why Congress should have delegated its authority or as a rationale for why it eventually did delegate. During the 1980s and 1990s, Executive branch officials indirectly used these arguments by regularly citing the disastrous period of Smoot-Hawley as an example of what would happen without a delegation of authority. However, as an explanatory tool for detailing the operation and formulation of trade policy prior to 1934, agency falls well short.

After 1934, however, agency seems to work well in several periods, in addition to the one under investigation here. In 1948, for example, the Reciprocal Trade Agreements Act that originally delegated negotiating authority to the President was again up for Congressional renewal. Much like the poisoned trade atmosphere of the 1980s, the mood of members of Congress in early 1948 was critical of Truman Administration trade policy as details of the recently concluded GATT negotiations emerged. Outraged by what it perceived to be the Administration's weakness at the GATT negotiations in giving away more trade concessions than it received from member countries, Congress significantly

circumscribed the President's negotiating authority.[240] As in the late 1980s, the principal in 1948 could have easily, and to some degree justifiably, revoked Executive negotiating authority altogether. Instead, the principal sought a revision in its contractual relationship with its agent, but, as agency both predicts and helps to understand, Congress sought a contract nevertheless.

However, not all institutional change in American foreign economic policy can be explained through agency. For example, Nixon Administration trade policy in the early 1970s, much like that of the first Reagan Administration, was in the midst of significant bureaucratic infighting, particularly between the Office of the USTR and the Department of Commerce, over which government department would take the lead in formulating and monitoring trade legislation. Rather than speaking with one voice on behalf of American trade interests, the USTR was too often just a small, at times isolated, component of confused economic policy coordination at home and abroad. As proposals for the elimination of the USTR were bantered about, the confusion they reflected over the roles of different agencies in the American system were strong evidence that the principal-agent relationship was at a dysfunctional stage.[241] Hence, while agency may be appropriate for an understanding of the reasoning behind institutional change to contractual relations between a principal and agent over trade policy, when agency breaks down, other, more descriptive lenses such as inter-branch or interest group politics models may need to be incorporated into an agency framework for an understanding of the intricacies of why agency is dysfunctional at all. For example, during the Nixon administration significant bureaucratic infighting, the relative absence of the USTR from important trade policy

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[240]Zeiler, *Free Trade, Free World*, 84-88, 125. Authority was cut to only one year, and Congress significantly increased the power of the Tariff Commission by requiring the President to submit lists of tariff reduction offers to the Commission where a "scientific" standard would be applied to determine peril points for individual industries. In other words, the Commission was charged with determining how far tariffs could be reduced before domestic industry was harmed by foreign imports.

[241]See Pastor, *Congress and the Politics*, 138-9; Dryden, *Trade Warriors*, chapters 7, 11.

initiatives such as the 1974 Trade Act, or even the August 1971 decision to abandon the gold standard all suggest a broken contractual principal-agent relationship.

We have seen how important agency was between 1985 and 1992, but what about agency as applied to the 1997 fast track debate in which the Clinton Administration was denied an extension of fast track authority? One assertion made in this paper is that agency evolved out of a need on the part of Congress for an agent to conduct trade policy on its behalf. While principal-agent relationships evolve in order to reduce transaction costs such as monitoring by the principal, institutional evolution does not guarantee the agent continuous delegation, nor necessarily a form of delegation that maintains liberal, open American trade policies. When the principal is faced with uncertainty regarding the activities of its agent, it will seek to create incentives or design institutional procedures that constrain the agent in the least costly manner available to ensure that actions taken by the agent yield the desired outcome. Throughout 1997, the USTR and other Administration officials repeated the familiar arguments about the need for fast track, this time to continue work on the ambitious Enterprise for the Americas Initiative.[242] Coming on the heels of NAFTA, the impact and full implementation of which was still years away, Congress, in denying fast track, may have sought a cooling off period for its agent. While a hemispheric free trade pact might be a long term goal, in 1997 Congress did not necessarily see it as being in the near term national interest to enter into substantive talks. Following 1994 mid-term elections, both houses of Congress were for the first time in more than a generation in Republican hands. Given the intensely partisan nature of

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[242]Prepared Testimony of Ambassador Charlene Barshefsky, United States Trade Representative, in U.S. Congress, Senate, Committee on Finance, 105th Congress, 1st session, June 3, 1997; Testimony of USTR Charlene Barshefsky, U.S. Congress, Senate, Committee on Finance, *Renewal of Fast Track Authority*, 105th Congress, 1st session, September 17, 1997; Statement of Deputy USTR Jeffrey Lang, U.S. Congress, House, Committee on Agriculture, Subcommittee on General Farm Commodities, *Renewal of Fast Track Authority and U.S. Agriculture*, 105th Congress, 1st session, September 23, 1997; Statement by Ambassador Lang, Deputy USTR, in U.S. Congress, Senate, Committee on Finance, Subcommittee on Trade, 105th Congress, 1st session, May 15, 1997.

Congressional-Executive relations thereafter, culminating in the historic 1998 impeachment proceedings against President Clinton, critics of agency as well as proponents of partisan politics approaches might again argue that Congressional Republicans hoped to thwart any initiatives put forward by the Clinton Administration, including fast track. Was partisan conflict responsible for the defeat of fast track in 1997? The charged political atmosphere in 1997 and 1998 obviously points to partisanship as a significant factor. However, on trade issues, the influence of partisan conflict over fast track in 1997 is ambiguous in light of evidence demonstrating that trade has seldom been a partisan issue in recent trade history.[243] Several other pieces of anecdotal evidence also cast doubt on partisan conflict as a cause for the failure of fast track in 1997. First, in the past two decades, the Republican party has been generally oriented toward a liberalized international trade regime. Second, although fast track renewal was a Clinton Administration request, the Enterprise for the America's Initiative, for which fast track authority was needed, had been a Bush Administration initiative. In fact, although Clinton was in office when both NAFTA (1993) and the Uruguay Round of the GATT (1994) (now the World Trade Organization) were given Congressional approval, Republicans had regularly claimed credit for progress toward trade liberalization and dated the origins of their support all the way back to the first Reagan Administration. Why would the Republican controlled Congress seek to scuttle further trade liberalization on the basis of partisan conflict after capturing the legislative momentum in 1994? Cast in a framework of agency, the 1997 fast track debate was more likely a product of a principal constraining its agent rather than partisan feuding. Denying fast track to the Administration simply became an institutional *dis*incentive to negotiate hemispheric agreements, or possibly emerged out of a desire to review the results of NAFTA and the Uruguay Round of the GATT, but was nevertheless still part of the "desired outcome" sought by the principal.

Skeptics of agency as a foreign trade policy lens could suggest that because "desired outcome" could mean just about anything, agency then becomes unfalsifiable

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[243]See above 93-94.

under any circumstance and loses its elegance as a theoretical approach. However, "desired outcome" should not be interpreted as a convenient way to hide theoretical deficiencies, but rather as a necessary part of the principal's decision-making process under conditions of uncertainty. Consider, once again, Hudson's Bay Company operations in seventeenth and eighteenth century British North America. What if after the first fifty years of trapping around Hudson's Bay, resource depletion had reached the point of diminishing returns? The "desired outcome" in the face of an uncertain future for the resource base might have been to end company operations around the Bay and go home. Rather than continuing to futilely alter principal-agent institutions to squeeze additional productivity out of a depleted resource base, the company could have concluded that it was time to simply end the principal-agent relationship around the Bay.[244] In other words, whether applied to the Hudson's Bay Company in early British North America or to the Congressional decision to deny fast track to the Administration in 1997, alterations in the principal-agent relationship in an effort to satisfy the desired outcome reflect the realities of economic uncertainty that may bring about a reevaluation of the necessity of agency.

Desired outcome also points positively to agency's elegance as a theoretical approach to American trade policies and its advantages, particularly since the end of the Cold War, over existing frameworks that have tried to explain trade policy within the broader context of foreign policy. Throughout the postwar period, much has been made of the global market place and how economies have become highly interdependent. The 1998 Asian financial crisis and efforts by the International Monetary Fund (IMF) to prevent its spread to Latin America were only the latest examples of that interdependence cited by those scholars who emphasize external, or systemic, determinants of foreign policy.

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[244]Ann Carlos and Frank Lewis have demonstrated that between 1700 and 1763, resource depletion was in fact a significant problem around Hudson's Bay, particularly as French competition emerged in the region. Although historians have held Natives responsible for over trapping, Carlos and Lewis demonstrate that the tragedy of the commons and Hudson's Bay Company policies contributed to resource depletion. Ann M. Carlos and Frank D. Lewis, "Indians, the Beaver, and the Bay: The Economics of Depletion in the Lands of the Hudson's Bay Company, 1700-1763," *Journal of Economic History* 53 (September 1993): 465-494.

Scholarship in this realm ranges widely and has emphasized everything from the growing importance of international financial and political bodies such as the IMF or the World Trade Organization (WTO) in shaping the economic patterns of national economies to conspiracy-like core-periphery depictions of an unequal and exploitive world economy dominated by powerful business interests in the developed world. While international bodies such as the IMF cannot be ignored and have had a dramatic impact on some of the world's largest economies, most recently Brazil, these bodies are also not the only determinants of trade policy. Even for small economies, national policy alternatives still exist in the face of growing interdependence. Although also enmeshed in an interdependent world, the United States, as the world's largest economic power, certainly has even more latitude to maneuver its own national policies. One difficulty with systemic approaches to American foreign policy is that they tend to assume that a limited set of factors contribute to trade policy outcomes. Scholars that emphasize the role of international institutions tend to ignore, particularly in the case of the United States, domestic economic policy processes and assume the predominance, or at least the growing influence, of international institutions . Leftist scholars who have examined the alleged exploitation of the developing world by the developed have too cynically assumed that the domestic decision making process has been corrupted by elite political or economic interests. Through agency, we have seen that while international bodies such as the GATT/WTO, the IMF, or even the United Nations play important roles in American policy formulation, they certainly are not the only, nor even the most important, factors in the policy process, nor do they necessarily infringe upon national sovereignty or become incompatible with the U.S. national interest. With agency as a framework, we have also seen how Congress, in effect, insulates itself from narrow, often localized, business interests seeking favorable trade legislation by delegating its authority over trade to the Executive. By doing so, Congress alleviates constituent pressure by transferring it to a body with a broader national constituency that is to some degree still under Congressional control, yields a trade policy that is different from that which Congress itself could have created.

Agency also helps further our understanding of how domestic sources of foreign trade policy formulation operate. Like advocates of those systems approaches that fail to acknowledge the complexities of the domestic process, those scholars who have emphasized the dominance of interest group politics have not acknowledged that through delegation interest group pressure is mitigated. Inter-branch or bureaucratic politics models go a long way toward capturing many important aspects of trade policy formulation, and in many ways mirror agency in emphasizing the interaction between Congress and the Executive. At the very least, these approaches capture aspects of the bargaining that often takes place within each branch of government. However, agency can incorporate both of these approaches while also considering more explicitly the importance of the systemic forces that also influence policy. Additionally, whereas interest group, inter-branch, and bureaucratic lenses all emphasize the importance of conflict and compromise in policy outcomes, agency argues for the existence of a more benign process of policy formulation based upon the reciprocal need for a principal-agent relationship. Agency serves as a corrective to the tendency of bureaucratic and inter-branch politics lenses to focus on foreign policy as the product of an Executive dominated policy apparatus where such ephemeral qualities as presidential leadership are considered to be key inputs to the policy process. While the broad foreign policy agenda is largely set by the Executive, agency cautions against applying such a broad brush to all aspects of foreign policy, especially trade. In the trade policy development examined by this study, agency demonstrates that Congress and the Executive each played important, mutually beneficial, and necessary roles in the policy process.

In the last several decades, scholars have increasingly moved toward a more complex, and more accurate, view of international relations, foreign policy, and foreign economic policy that looks for the sources of foreign policy in a variety of areas. However, agency cautions scholars against lumping foreign economic policy so readily together with broader foreign policy issues. Although national security and economic security are intimately linked in many ways, the formulation of economic policies in the United States should be considered separately from national security, especially in the

modern post-Cold War international environment. For example, although post-revisionist diplomatic historians pay considerable attention to both the domestic and international complexities of the foreign policy process, their central thesis that domestic economic considerations have been regularly subordinated to broader national security issues implies a unitary decision making process centered around the Executive branch. In reality, foreign economic policy in the entire postwar period has been much more the product of a contractual agency relationship than it has been the result of an Executive dominated decision making process in that the principal has regularly checked Executive branch discretion in arbitrarily subordinating domestic economic interests to larger foreign policy goals. Recent history, in particular, suggests that the Executive's discretion to unilaterally trade away economic concessions in favor of foreign policy objectives has been weakened in the 1980s and 1990s and likely will be curtailed significantly in the future. As we have seen, Congress took steps to eliminate such Executive discretion through provisions such as Section 301 contained in the 1988 Omnibus Act, toughened its oversight of the Executive, and asserted its right to rescind existing fast track authority at any time. Congress's 1997 refusal to extend fast track negotiating authority to the Clinton Administration provided further evidence of contemporary Congressional reluctance to blindly extend trade policy authority to the Executive.

Finally, and perhaps most importantly, while agency advances our understanding of why and through what means Congress seeks to constrain its agent, it also contributes to our appreciation of how Congressional constraints are also coupled with positive incentives. Congressional-Executive relations are characterized by much more than negative checks by Congress on Executive actions. In fact, as this study suggests, the agent is at least as important to the principal as the principal is to the agent. Regardless of one's interpretation of how America came to be one of the most important political, military, and economic forces of the twentieth century, the United States has for most of this century required an outward-looking foreign policy to protect its interests around the world. Where trade is concerned the authority for that presence rests with Congress. Since foreign economic policy conducted by a committee of more than four-hundred Members

of Congress is impractical, and even undesirable given the negative message divided foreign policy responsibilities could send abroad, that power must be delegated; and with delegation comes agency.

Nearly half a century ago, Friedrich Hayek warned of the dangers to political and economic freedom intrinsic in collectivist tendencies toward social, economic, and political planning.[245] As more and more countries throughout the world struggle with development issues and attempt to break free from the shackles of planned economies, the tensions often inherent in reconciling the political and economic goals of national development with the desire for the liberalism of the free market will challenge economies the world over. Even among industrial economies, challenges to economic prosperity abound. Governments, already one of the largest economic forces in the free market, have throughout the twentieth century been expected to help create the conditions for national prosperity. Many of the most popular economic catch phrases such as free trade, open markets, and globalization all imply economic patterns free from the influence of government strictures. In reality, even among developed nations, the struggle to maintain their economic positions relative to each other and the developing world will generate increasing pressure on political leaders to develop policies that continue to promote prosperity. While tariffs have ceased to be the most significant barriers to world economic flows, non-tariff barriers have supplanted them as the major distortions to trade. Addressing non-tariff barriers at future trade negotiations has often been compared to the many problems associated with draining a swamp. Because non-tariff barriers not only include measures such as government export subsidies and quotas intended to have a direct impact on trade flows, but also those such as safety, health or pollution standards, or regional development subsidies, whose purpose and orientation are primarily domestic but which nevertheless have an impact abroad. Given that many of these policies are intimately tied to domestic policies with all their social, cultural, political, environmental, and economic implications, these subjects have become, and will continue being,

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[245]Friedrich A. Hayek, *The Road to Serfdom* (Chicago: University of Chicago Press, 1944).

extremely contentious issues in future economic relations. In recent years, for example, the so-called industrial policies of many nations, especially those of Japan and Germany, have generated renewed interest among both scholars and policy makers. Some have even called upon the United States to move its national policies toward a more cooperative effort between business, government, and the research community to identify and actively shift economic activity toward emerging technologies.[246] The debate over the market distorting effects of the intimate working relationship between the business, banking, and government sectors of the Japanese economy in particular led in 1989 to the United States initiated Structural Impediments Initiative aimed at addressing and eliminating some of these distortions.

Understanding the complexities of these issues, how they are created, maintained, and supported by the cultural, political, and economic imperatives of a society will be an important key to the larger questions of peaceful political and economic development in both the developed and developing worlds. Understanding how national economic policies and non-tariff barriers are dealt with by each of the world's economies will be of major importance in the years to come as economic issues grow in importance. However, because the United States has been a premier economic power in the mid and late twentieth century, and appears poised to remain so for the foreseeable future, understanding how non-tariff barriers and other economic issues play themselves out within the U.S. political system will be of paramount importance to understanding broader patterns of world economic activity.

Agency as a framework for understanding American policy choices supports this effort in three important ways. First, agency is a parsimonious, descriptive, explanatory, and to some extent predictive lens for viewing American foreign economic policy in many different periods. It offers a plausible economic, rather than purely political, rationale for the interaction between principal and agent that results in policy formation. Second, unlike Congressional or Executive dominance decision-making models that depict Congress and

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[246]See D'Andrea Tyson, *Who's Bashing Whom?*, 286-295.

the Executive as being in a pitched battle over mutually exclusive positions, agency offers a more benign explanation for compromise that explains why in the midst of the mid-1980s and early 1990s acrimony over American economic policies and pressure to adopt nationalistic policies, American policy retained its essentially liberal orientation. Third, and most interestingly, agency helps explain why the American foreign economic policy process regularly manages to come up with "middle ground" policy choices. Whereas inter-branch politics models suggest that middle ground policies are the product of bitter debate and compromise, agency asserts that through the deliberate delegation to an agent, the American system generates policy options and outcomes that neither Congress nor the Executive could have created had either been left to formulate them on their own.

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